Legislative Audit Division

State of Montana

Report to the Legislature

January 2003

Financial-Compliance Audit

For the Two Fiscal Years Ended June 30, 2002

Public Employees' Retirement Board

A component unit of the state of Montana

We performed a financial-compliance audit of the Public Employees' Retirement Board for the two fiscal years ended June 30, 2002. This report contains two recommendations related to the actuarial soundness of the Game Wardens' and Peace Officers' Retirement System and recording license and registration fees on the state's accounting records.

This report also contains the financial statements and our independent auditor's report for the Public Employees' Retirement Board for the fiscal year ended June 30, 2002. These statements demonstrate the financial position and results of operations for the following pension trust funds:

Public Employees' Retirement System
Municipal Police Officers' Retirement System
Game Wardens' and Peace Officers' Retirement System
Sheriffs' Retirement System
Judges' Retirement System
Highway Patrol Officers' Retirement System
Firefighters' Unified Retirement System
Volunteer Firefighters' Compensation Act
Section 457 Deferred Compensation Plan

The financial audit of the Public Employees' Retirement Board's financial statements for the fiscal year ended June 30, 2001, was issued in a separate report in November 2001 (01-08).

Direct comments/inquiries to:
Legislative Audit Division
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02-08

FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Legislative Audit Division to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these reporting requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2003, will be issued by March 31, 2004. The Single Audit Report for the two fiscal years ended June 30, 2001, was issued on March 26, 2002. Copies of the Single Audit Report, when available, can be obtained by contacting:

Single Audit Coordinator
Office of Budget and Program Planning
State Capitol
Helena MT 59620
Phone (406) 444-3616

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January 2003

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial-compliance audit report on the Public Employees' Retirement Board (PERB), a component unit of the state of Montana, for the two fiscal years ended June 30, 2002. Included in this report are two recommendations related to the actuarial soundness of the Game Wardens' and Peace Officers' Retirement System and recording license and registration fees on the state's accounting records.

We issued an unqualified opinion on the PERB's financial statements for the fiscal year ended June 30, 2002. An unqualified opinion means a reader can rely on the information presented in the financial statements.

Our unqualified audit opinion on the financial statements is also contained in the PERB Comprehensive Annual Financial Report. Copies of the PERB's annual report for fiscal year 2001-02 can be obtained from the Public Employees' Retirement Administration (PERA). The annual report contains background, statistical, and actuarial information that is not included in this audit report which may be of interest to legislators or the public.

The written response to the audit recommendations is included at the end of the audit report. We thank the executive director and his staff for their assistance and cooperation.

Respectfully submitted,

(Signature on File)

Scott A. Seacat
Legislative Auditor

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Legislative Audit Division

Financial-Compliance Audit
For the Two Fiscal Years Ended June 30, 2002

Public Employees' Retirement Board

A component unit of the state of Montana

Members of the audit staff involved in this audit were Jeane Carstensen-Garrett, Cindy S. Jorgenson, Amber Long, Laura L. Norris, Jeff Tamblyn, and Alexa O'Dell.

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Appointed and Administrative Officials

Public Employees' Retirement Board

		Term Expires
Terry Teichrow, President	Helena	3/31/05
Carole Carey, Vice President	Ekalaka	3/31/07
Robert Griffith	Helena	3/31/03
N. Jay Klawon	Hamilton	3/31/04
Carol Lambert	Hammond	3/31/06
Troy McGee	Helena	3/31/03
Jean Thompson	Billings	3/31/04

Administrative Officials

Mike O'Connor, Executive Director

Kim Flatow, Member Services Bureau Chief

Roxanne Minnehan, Fiscal Services Bureau Chief

Kathy Samson, Defined Contribution Plans & Educational Services Bureau Chief

For additional information concerning the Montana Public Employees' Retirement Board, contact Mike O'Connor, Executive Director, at:

100 North Park Avenue Suite 220
PO Box 200131
Helena MT 59620-0131
(406) 444-3154

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Public Employees' Retirement Board

This report contains the results of our financial-compliance audit of the Public Employees' Retirement Board (PERB) for the two fiscal years ended June 30, 2002. We issued an unqualified opinion on the financial statements for the fiscal year ended June 30, 2002. This means the reader may rely on the financial information presented. The financial audit of the PERB's financial statements for the fiscal year ended June 30, 2001 was issued in a separate report in November 2001 (01-08).

Public Employees' Retirement Administration (PERA) personnel prepare PERB financial statements from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. Adjustments are made to properly present financial activity to the readers of the statements.

This report contains two recommendations related to the actuarial soundness of the Game Wardens' and Peace Officers' Retirement System and recording license and registration fees on the state's accounting records. The previous financial-compliance audit report for the two fiscal years ended June 30, 2000, contained four recommendations to PERB.

The listing below serves as a means of summarizing the recommendations contained in the report, the PERB's response thereto, and a reference to the supporting comments.

Recommendation #1

We recommend the PERB immediately reassess the assumptions for the Game Wardens' and Peace Officers' Retirement System in order to introduce legislation, if any, needed to ensure the system is actuarially sound as required by the Montana Constitution and state law.....................................8

PERB Response: Concur. See Page B-3.

Recommendation #2

We recommend PERA work with the Department of Administration to ensure state accounting policy results in the proper and complete implementation of Generally Accepted Accounting Principles. 9

PERB Response: Concur. See page B-4.

Introduction

We performed a financial-compliance audit of the Public Employees' Retirement Board (PERB) for the two fiscal years ended June 30, 2002. The objectives of our audit were to:

1. Determine PERB's compliance with applicable laws and regulations.
2. Recommend improvements in PERB's management and internal controls.
3. Determine if the financial statements prepared by the Public Employees' Retirement Administration (PERA) fairly present PERB's financial position as of June 30, 2002, and the changes in its financial status for the fiscal year then ended, in conformity with generally accepted accounting principles.
4. Determine the status of prior audit recommendations.

The financial audit of the PERB's financial statements for the fiscal year ended June 30, 2001 was issued in a separate report in November 2001 (01-08).

PERA prepares PERB's financial statements from the Statewide Accounting, Budgeting, and Human Resources System (SABHRS) with adjustment. Adjustments are made to accurately present financial activity to the readers of the statements.

This report contains two recommendations. Other areas of concern deemed not to have a significant effect on the successful operation of PERB are not specifically included in the report, but have been discussed with management. In accordance with section 5-13-307, MCA, we analyzed the cost of implementing the recommendations contained in this report and determined it was not significant.

Background

The PERB is a component unit of the state of Montana. A component unit is a legally separate organization for which the state of Montana is financially accountable. The PERB has exclusive control of the funds of seven retirement systems and the Volunteer

Firefighters' Compensation Act, as well as the Section 457 Deferred Compensation Plan. The PERB governs PERA, which is responsible for daily administration of the retirement systems. The governor appoints the seven board members to five-year terms.

Retirement Systems and Compensation Act

PERB manages the activities of the following pension trust funds:

- Public Employees' Retirement System
- Municipal Police Officers' Retirement System
- Game Wardens' and Peace Officers' Retirement System
- Sheriffs' Retirement System
- Judges' Retirement System
- Highway Patrol Officers' Retirement System
- Firefighters' Unified Retirement System
- Volunteer Firefighters' Compensation Act

Except for the Public Employees' Retirement System, the retirement systems are solely defined benefit systems providing pension, disability and death benefits to members. Effective July 1, 2002, the Public Employees' Retirement System provides both defined benefit and defined contribution plan options to its members. In a defined contribution plan, monthly benefits are based on accumulated contributions and investment earnings. In a defined benefit plan, monthly benefits are based on years of service and salary levels while still employed. The Volunteer Firefighters' Compensation Act provides pension, disability and death benefits to volunteer firefighters who are members of eligible Montana volunteer fire companies. Monthly benefits are based on years of service.

PERB obtains an actuarial valuation of each of the retirement systems and the Volunteer Firefighters' Compensation Act biennially, the most recent of which was as of July 1, 2002. The purpose of the valuation is to determine the unfunded accrued liabilities for each of the retirement systems and the Volunteer Firefighters' Compensation Act based on their various present and prospective assets and liabilities. Except for the Game Wardens' and Peace Officers' Retirement System, PERB's actuary considers the

defined benefit retirement systems and the Volunteer Firefighters' Compensation Act to be actuarially sound.

Section 457 Deferred Compensation Plan

The Section 457 Plan allows employees to set aside a portion of their salary each payday toward retirement while deferring state and federal income taxes until future years. Participating employees have two investment options:

- the fixed option, which guarantees both principal (contributions) and a pre-established quarterly rate of earnings;
- the variable option, which consists of numerous mutual funds.

Participating employees are allowed to invest in both the fixed and variable options. Those participating in the variable option may invest in as many offered funds as desired. Withdrawal of deferred compensation funds is only available to employees upon separation from state service, retirement, death, or upon an unforeseeable emergency meeting IRS-specified criteria while still employed.

Prior Audit Recommendations

The financial-compliance audit report for the two fiscal years ended June 30, 2000, contained four recommendations to the PERB. The recommendations addressed incomplete and inaccurate accounting for pension and deferred compensation activity, timeliness of cash deposits, and state debt. During the financial audit for the fiscal year ended June 30, 2001, we determined the PERB implemented the recommendations related to accounting for pension and deferred compensation activity. During the current audit, we determined the PERB implemented the recommendation on timeliness of cash deposits, but did not implement the recommendation related to state debt. The following paragraphs outline the current status of this issue.

Defined Contribution Long-Term Loan

Chapter 471, Laws of 1999, authorized the PERB to obtain a loan from the INTERCAP Revolving Loan Program to pay startup costs of the Defined Contribution (DC) Plan. The Department of Administration entered into a 10-year loan agreement with the Board of Investments on June 16, 2000 for this purpose. As of June 30, 2002, the PERB has drawn $1,498,000 under this loan agreement. DC Plan revenues, consisting of employer and employee contributions and investment earnings, are irrevocably pledged for the repayment of the loan. The DC Plan revenues are considered state revenues. Because state revenues are pledged for repayment, we believe the use of the INTERCAP Revolving Loan Program to fund the startup costs constitutes state debt.

Article VIII, Section 8, of the Montana Constitution prohibits the creation of state debt unless authorized by a two-thirds vote of each house of the legislature. Chapter 471, Laws of 1999, did not receive a two-thirds vote in the House of Representatives. As such, we believe the establishment of this loan violates the constitution.

In our prior audit we recommended the PERB seek legislative direction in order to resolve these concerns. These concerns have not been resolved by PERB. PERA personnel do not believe the loan constitutes state debt and do not agree that corrective action is necessary in this situation. We believe the PERB should take

appropriate measures to resolve this issue, which may include obtaining an Attorney General's opinion on whether the loan represents state debt or seeking legislative authorization of the loan as required by the Constitution.

Game Wardens' and Peace Officers' Retirement System Soundness

Article VIII, Section 15, of the Montana Constitution requires the retirement plans to be funded on an actuarially sound basis. State law indicates a defined benefit retirement system is actuarially sound when its contributions are sufficient to pay the full actuarial cost of the plan.

The results of the July 1, 2002 actuarial valuation indicate the Game Wardens' and Peace Officers' Retirement System (GWPORS) is not actuarially sound. Specifically, the contribution rates established in state law are insufficient. The combined contribution rate necessary to maintain actuarial soundness of the plan is 20.82 percent. The combined statutorily required employer and employee contributions are currently 19.56 percent of salaries, which is 1.26 percent lower than necessary to maintain the plan's actuarial soundness.

According to PERA personnel, a change in the plan's membership requirements resulted in a significant number of state correctional officers electing membership in GWPORS rather than the Public Employees' Retirement System. PERA personnel currently do not intend to seek legislation to modify the contribution rates because they have not had an opportunity to analyze whether the change in membership will have a long-term impact on the actuarial soundness of the system. PERA personnel requested their actuary to review the appropriateness of the assumptions used for the valuation in light of the demographic changes occurring in the system. According to PERA personnel, correctional officers traditionally withdraw their contributions prior to retirement more often than other members of the system. PERA personnel do not have an estimate of when that analysis will be complete. We believe the PERB should immediately determine whether the GWPORS assumptions should be modified for the demographic changes and whether any proposed modifications would, in fact, reduce the combined contribution rate needed to maintain the plan's actuarial soundness. We believe this is necessary to facilitate the introduction of legislation, if any, needed to make the system actuarially sound.

Recommendation #1
We recommend the PERB immediately reassess the assumptions for the Game Wardens' and Peace Officers' Retirement System in order to introduce legislation, if any, needed to ensure the system is actuarially sound as required by the Montana Constitution and state law.

License and Registration Fees

The state of Montana is required to make contributions for highway patrol officers to the Highway Patrol Officers' Retirement System (HPORS). Some of these contributions are paid by the Department of Justice from license fees collected by that agency. Another portion is paid by the Department of Administration from vehicle registration fees. In fiscal year 2001-02, these contributions were $798,912 and $308,973, respectively. The PERA, on recommendation from the Department of Administration and in accordance with state accounting policy issued July 2, 2002, recorded this activity as transfers-in on the state's accounting records.

State law requires the PERA to record its financial activity on the state's accounting records in accordance with generally accepted accounting principles (GAAP). The PERB is a discretely presented component unit of the state of Montana. This means the PERB is a separate legal entity for financial reporting purposes. Because of this relationship, GAAP requires the contributions be recorded as revenue by PERA and expenditures by the Departments of Justice and Administration, rather than as transfers. We believe current state accounting policy does not properly or completely implement current GAAP for transactions between the state and its discretely presented component units. While these contributions are appropriately reported on the PERB's financial statements, the underlying accounting records do not properly account for the activity.

PERA personnel indicated they do not believe state accounting policy is correct in this situation, but that they are required to comply with it. We believe the PERA should work with the Department of

Administration to resolve this issue and ensure state accounting policy addresses current GAAP.

Recommendation #2
We recommend PERA work with the Department of Administration to ensure state accounting policy results in the proper and complete implementation of Generally Accepted Accounting Principles.

Independent Auditor's Report & PERB Financial Statements

LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
John W. Northey, Legal Counsel

Deputy Legislative Auditors:
Jim Pellegrini, Performance Audit
Tori Hunthausen, IS Audit & Operations
James Gillett, Financial-Compliance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Combined Statement of Fiduciary Net Assets-Pension Trust Funds of the Public Employees' Retirement Board, a component unit of the state of Montana, as of June 30, 2002, and the related Combined Statement of Changes in Fiduciary Net Assets-Pension Trust Funds for the fiscal year then ended. These financial statements are the responsibility of the Public Employees' Retirement Board. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Public Employees' Retirement Board as of June 30, 2002, and the changes in fiduciary net assets for the fiscal year then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in note D, the Game Wardens' and Peace Officers' Retirement System is not considered actuarially sound as required by Article VIII, Section 15, of the Montana Constitution and state law.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements of the Public Employees' Retirement Board. The Schedules of Administrative Expenses, Investment Expenses, and Consultants are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit

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of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Management's Discussion and Analysis, the Schedules of Funding Progress, and Employer Contributions & Other Contributing Entities are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Respectfully submitted,

(Signature on File)

James Gillett, CPA
Deputy Legislative Auditor

November 13, 2002

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Public Employees' Retirement Board

A Component Unit of the State of Montana

Management's Discussion and Analysis

This section presents management's discussion and analysis of the Montana Public Employees' Retirement Board's financial presentation and performance of the plans administered by the Board for the year ending June 30, 2002. It is presented as a narrative overview and analysis of the financial statements and other information which are presented in the Financial Section of this Component Unit Financial Report.

Financial Highlights

- *The Montana Public Employees' Retirement Board's combined total net assets of the defined benefit plans decreased by $248 million or 7.5 percent in fiscal year 2002. The decrease was primarily due to the downturn in equity markets and increasing benefit payments.*

- *The Montana Public Employees' Retirement Board's defined benefit plans were actuarially funded at an average of 93.6 percent as of July 1, 2002, a decrease over the comparative of 114.5 percent as of July 1, 2000. The decrease in funding is primarily due to the downturn in the equity markets and an increase in retirees and benefit enhancements.*

- *The Montana Public Employees' Retirement Board's defined contribution plans combined total net assets decreased by $4.3 million or 2.2 percent in fiscal year 2002. The total decrease in Net Assets was partially offset by increased contributions from participants.*

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Public Employees' Retirement Board's (PERB) financial reporting which is comprised of the following components:

(1) Financial Statements
(2) Notes to the Financial Statements
(3) Required Supplementary Information

Collectively, this information presents the combined net assets held in trust for pension benefits for each of the plans administered by the Public Employees' Retirement Board as of June 30, 2002. This financial information also summarizes the combined changes in net assets held in trust for pension benefits for the year then ended. The information in each of these components is briefly summarized as follows:

(1) Financial Statements. For the fiscal year ended June 30, 2002, financial statements are presented for the fiduciary funds administered by the PERB. Fiduciary funds

are used to account for resources held for the benefit of parties outside of the PERB. The fiduciary fund is comprised of eight defined benefit plans and two defined contribution plans.

- The Statement of Fiduciary Net Assets is presented for the pension trust funds at June 30, 2002. These financial statements reflect the resources available to pay benefits to retirees and beneficiaries, at the end of the year reported.

- The Combined Statement of Changes in Fiduciary Net Assets is presented for the pension trust funds for the year ended June 30, 2002. These financial statements reflect the changes in the resources available to pay benefits to retirees and beneficiaries, for the fiscal year 2002.

(2) Notes to the Financial Statements. The Notes to the Financial Statements provide additional information that is essential for a full understanding of the data provided in the financial statements. Information in the Notes to the Financial Statements is described below:

- Note A provides a summary of significant accounting policies, including the basis of accounting, property and equipment used in operations, methods used to value investments, summaries of our investment vendors and other significant accounting policies or explanations.

- Note B provides information about litigation.

- Note C describes the debt obligation of the PERS-DCRP. This is the implementation loan for the PERS-DCRP that is to be paid back over ten years.

- Note D describes the plans' membership and descriptions of the plans administered by the Public Employees' Retirement Board. Summaries of benefits and contribution information are also provided.

(3) Required Supplementary Information. The required supplementary information consists of the schedules of funding status and required contributions and related notes concerning actuarial information of the defined benefit pension plans administered by the PERB.

Financial Analysis of the Systems – Defined Benefit Plans

Investments

The Montana Board of Investments, as authorized by state law, invests the defined benefit plans' assets in investment pools. Each plan owns an equity position in the pools and receives proportionate investment income from the pool in accordance with respective ownership. The investment pools are: Montana Stock Pool, Retirement Fund Bond Pool, Montana International Pool, Montana Short Term Investment Pool, Montana Private Equity Pool and the Equity Index Fund. Each plan's allocated share of the investment in the pools is shown in the Statement of Net Assets of the plan. Investment gains and losses are reported in the Statement of Changes in Net Assets.

Defined Benefit Plans Total Investments

At June 30, 2002, the PERB's defined benefit plans held total investments of $3.0 billion, a decrease of $199.9 million from fiscal year 2001 investment totals. On the following pages are the schedules of Net Assets and Changes in Net Assets for the defined benefit plans.

Net Assets - Defined Benefit Plans

As of June 30, 2002 - and comparitive totals for June 30, 2001

(dollars in thousands)

	PERS		MPORS		GWPORS		SRS	
	2002	2001	2002	2001	2002	2001	2002	2001
Assets:								
Cash and Receivables	85,220	115,381	9,032	9,544	2,033	1,446	4,349	6,600
Securities Lending Collateral	127,173	113,424	6,460	5,639	1,757	1,492	6,417	5,587
Investments	2,494,337	2,664,519	110,998	117,984	30,490	31,766	111,550	117,330
Property and Equipment	2	3						
Total Assets	2,706,732	2,893,327	126,490	133,167	34,280	34,704	122,316	129,517
Liabilities:								
Secuity Lending Collateral	127,173	113,424	6,460	5,639	1,757	1,492	6,417	5,587
Other Payables	14,291	1,158	50	59	67	42	431	53
Total Liabilities	141,464	114,582	6,510	5,698	1,824	1,534	6,848	5,640
Total Net Assets	2,565,268	2,778,745	119,980	127,469	32,456	33,170	115,468	123,877

Changes In Net Assets - Defined Benefit Plans

For the year ended June 30, 2002 - and comparative totals for June 30, 2001

(dollars in thousands)

	PERS		MPORS		GWPORS		SRS	
	2002	2001	2002	2001	2002	2001	2002	2001
Additions:								
Contributions	116,910	111,708	11,973	11,077	3,441	2,672	4,928	4,489
Operating Income		26						
Investment Income (Loss)	(201,365)	(148,518)	(9,220)	(6,165)	(2,564)	(1,598)	(9,152)	(6,379)
Total Additions	(84,455)	(36,784)	2,753	4,912	877	1,074	(4,224)	(1,890)
Deductions:								
Benefits	114,663	101,546	9,845	9,125	1,230	1,235	3,700	3,294
Refunds	11,048	12,063	348	430	331	217	446	377
Administrative Expenses	3,310	2,275	49	55	30	30	40	43
Miscellaneous Expenses		7						
Prior Period Adjustment		12						
Total Deductions	129,021	115,903	10,242	9,610	1,591	1,482	4,186	3,714
Increase (decrease) in net assets	(213,476)	(152,687)	(7,489)	(4,698)	(714)	(408)	(8,410)	(5,604)

Analysis of Individual Systems

PERS - DBRP and Education

The PERS-DBRP provides retirement, disability, and death benefits to covered employees of State, university system and local governments and certain employees of the school districts. Member and employer contributions and earnings on investments fund the benefits of the plan. The PERS-DBRP and the Education Fund have been combined in these comparisons. The PERS-DBRP net assets held in trust for benefits at June 30, 2002 amounted to $2.6 billion, a decrease of $213.5 (7.7 percent) from 2.8 billion at June 30, 2001.

Additions to the PERS-DBRP net assets held in trust for benefits include employer, mem-

JRS		HPORS		FURS		VFCA		TOTAL		Total %
2002	2001	2002	2001	2002	2001	2002	2001	2002	2001	Change
1,214	1,318	1,217	2,944	7,930	9,355	1,897	1,260	112,892	147,848	-23.6%
2,067	1,855	3,800	3,411	6,163	5,353	1,012	1,009	154,849	137,770	12.4%
36,139	39,340	66,580	71,710	105,987	111,885	15,021	16,486	2,971,102	3,171,020	-6.3%
								2	3	-33.3%
39,420	42,513	71,597	78,065	120,080	126,593	17,930	18,755	3,238,845	3,456,641	-6.3%
2,067	1,855	3,800	3,411	6,163	5,353	1,012	1,009	154,849	137,770	12.4%
4	5	20	29	43	53	133	42	15,039	1,441	943.7%
2,071	1,860	3,820	3,440	6,206	5,406	1,145	1,051	169,888	139,211	22.0%
37,349	40,653	67,777	74,625	113,874	121,187	16,785	17,704	3,068,957	3,317,430	-7.5%

JRS		HPORS		FURS		VFCA		TOTAL		Total %
2002	2001	2002	2001	2002	2001	2002	2001	2002	2001	Change
1,312	1,199	3,772	3,693	10,160	9,483	1,134	1,003	153,630	145,324	5.7%
									26	-100.0%
(3,047)	(2,162)	(5,590)	(3,828)	(8,845)	(5,997)	(591)	(260)	(240,374)	(174,907)	37.4%
(1,735)	(963)	(1,818)	(135)	1,315	3,486	543	743	(86,744)	(29,557)	193.5%
1,566	1,431	4,861	4,624	8,507	8,018	1,411	882	145,783	130,155	12.0%
		149	86	81	44			12,403	13,217	-6.2%
4	4	20	22	39	43	38	42	3,530	2,514	40.4%
						13	12	13	19	-31.6%
								0	12	-100.0%
1,570	1,435	5,030	4,732	8,627	8,105	1,462	936	161,729	145,917	10.8%
(3,305)	(2,398)	(6,848)	(4,867)	(7,312)	(4,619)	(919)	(193)	(248,473)	(175,474)	41.6%

ber, and state contributions and investment income. For the fiscal year ended June 30, 2002, contributions increased from $111.7 million in fiscal year 2001 to $116.9 million for an increase of $5.2 million (4.7 percent). Contributions increased because the number of participating employers increased and the number of members contributing to the plan increased. The plan recognized a net investment loss of $201.4 million for the fiscal year ended June 30, 2002 compared with a net investment loss of $148.5 million for the fiscal year ended June 30, 2001. The decreases in investment income are mainly due to the downturn in equity markets.

Deductions from the PERS-DBRP net assets held in trust for benefits primarily include re-

tirement benefits, refunds and administrative expenses. For fiscal year 2002, benefits amounted to $114.7, an increase of $13.1 million (12.9 percent) from fiscal year 2001. The increase in benefit payments was due to benefit enhancements enacted by the 2001 Legislature and an increase in benefit recipients. For fiscal year 2002, the costs of administering the plan's benefits amounted to $3.3 million, an increase of $1.1 million (54.5 percent) from fiscal year 2001. The increase in administrative expenses for the fiscal year 2002 was due to the beginning of the education program to educate PERS-DB members regarding the choice of the PERS-DBRP or the PERS-DCRP.

An actuarial valuation of the PERS-DBRP assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 99.97 percent from 125.07 percent at July 1, 2000. The PERS-DBRP actuarial assets were less than actuarial liabilities by $983 thousand at July 1, 2002, compared with $569.9 million surplus at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a result of the benefit enhancements enacted by the 2001 Legislature and the previous 4-year investment performance.

MPORS

The MPORS provides retirement, disability and death benefits to municipal police officers employed by first and second-class cities and other cities that adopt the plan. Member, employer and state contributions and earnings on investments fund the benefits of the plan. The MPORS net assets held in trust for benefits at June 30, 2002 amounted to $120.0 million, a decrease of $7.5 million (5.9 percent) from 127.5 million at June 30, 2001.

Additions to the MPORS net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, 2002, contributions increased from $11.1 million in fiscal year 2001 to $12.0 million, for an increase of $896 thousand (8.1 percent). Contributions increased because the number of participating employers increased and the number of members contributing to the plan increased. Contributions also increased because the total compensation reported for active members increased. The plan recognized a net investment loss of $9.2 million for the fiscal year ended June 30, 2002 compared with a net investment loss of $6.2 million for fiscal year ended June 30, 2001. The decreases in investment income are primarily due to the downturn in equity markets.

Deductions from the MPORS net assets held in trust for benefits mainly include retirement benefits, refunds and administrative expenses. For fiscal year 2002, benefits amounted to $9.8 million, an increase of $720 thousand (7.9 percent) from fiscal year 2001. The increase in benefit payments was due to benefit enhancements enacted by the 2001 Legislature and an increase in benefit recipients. For the fiscal year 2002, the costs of administering the plan's benefits amounted to $49 thousand, a decrease of $6 thousand (10.9 percent) from fiscal year 2001.

An actuarial valuation of MPORS assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 63.27 percent from 71.68 percent at July 1, 2000. The MPORS actuarial assets were less than actuarial liabilities by $83.3 million at July 1, 2002, compared with $51.3 million actuarial li-

abilities at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a result of the benefit enhancements enacted by the 2001 Legislature and the previous 4-year investment performance.

GWPORS

The GWPORS provides retirement, disability and death benefits to game wardens, warden supervisory personnel and state peace officers. Member and employer contributions and earnings on investments fund the benefits of the plan. The GWPORS net assets held in trust for benefits at June 30, 2002 amounted to $32.5 million, a decrease of $714 thousand (2.1 percent) from 33.2 million at June 30, 2001.

Additions to the GWPORS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, 2002, contributions increased from $2.7 million in fiscal year 2001 to $3.4 million, for an increase of $769 thousand (28.8 percent). Contributions increased because contribution rates for members increased and the number of currently employed members for whom contributions are paid increased due to the expansion of membership to include all state peace officers. The plan recognized a net investment loss of $2.6 million for the fiscal year ended June 30, 2002 compared with a net investment loss of $1.6 million for the fiscal year ended June 30, 2001. The decreases in investment income are mainly due to the downturn in equity markets.

Deductions from the GWPORS net assets held in trust for benefits mainly include retirement benefits, refunds and administrative expenses. For fiscal year 2002, benefits amounted to $1.2 million, a decrease of $5 thousand (0.4 percent) from fiscal year 2001. For fiscal year 2002, the cost of administering plan benefits amounted to $30 thousand, the same as for fiscal year 2001.

An actuarial valuation of GWPORS assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 99.03 percent from 137.81 percent at July 1, 2000. The GWPORS actuarial assets were less than actuarial liabilities by $379 thousand at July 1, 2002, compared with $9.0 million actuarial surplus at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a result of the benefit enhancements enacted by the 2001 Legislature, the expansion of the plan to all state peace officers and the previous 4-year investment performance.

SRS

The SRS provides retirement, disability and death benefits to all Department of Justice criminal investigators hired after July 1, 1993 and all Montana sheriffs. Member and employer contributions and earnings on investments fund the benefits of the plan. The SRS net assets held in trust for benefits at June 30, 2002 amounted to $115.5 million, a decrease of $8.4 million (6.8 percent) from 123.9 million at June 30, 2001.

Additions to the SRS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, 2002, contributions increased from $4.5 million in fiscal year 2001 to $4.9 million, for an increase of $439 thousand (9.8 percent). Contributions increased because the number of participating members contributing to the plan increased and the total compensation reported for active members increased. The plan recognized a net investment loss of $9.2 million for fiscal year ended June 30, 2002 com-

pared with a net investment loss of $6.4 million for the fiscal year ended June 30, 2001. The decreases in investment income are mainly due to the downturn in equity markets.

Deductions from the SRS net assets held in trust for benefits mainly include retirement benefits, refunds and administrative expenses. For fiscal year 2002, benefits amounted to $3.7 million, an increase of $406 thousand (12.3 percent) from fiscal year 2001. The increase in benefit payments was due to benefit enhancements enacted by the 2001 Legislature and an increase in benefit recipients. For fiscal year 2002, the costs of administering the plan's benefits amounted to $40 thousand, a decrease of $3 thousand (7.0 percent) from fiscal year 2001.

An actuarial valuation of SRS assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 113.95 percent from 143.83 percent at July 1, 2000. The SRS actuarial assets were more than actuarial liabilities by $17.0 million at July 1, 2002, compared with $38.5 million actuarial surplus at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a result of the benefit enhancements and member expansion enacted by the 2001 Legislature and the previous 4-year investment performance.

JRS

The JRS provides retirement, disability and death benefits to all Montana judges of the district courts, justices of the Supreme Court and the Chief Water Judge. Member and employer contributions and earnings on investments fund the benefits of the plan. The JRS net assets held in trust for benefits at June 30, 2002 amounted to $37.3 million, a decrease of $3.3 million (8.1 percent) from 40.7 million at June 30, 2001.

Additions to the JRS net assets held in trust for benefits include member and employer contributions and investment income. For the fiscal year ended June 30, 2002, contributions increased from $1.2 million in fiscal year 2001 to $1.3 million in fiscal year 2002, for an increase of $113 thousand (9.4 percent). Contributions increased because the total compensation reported for active members increased. The plan recognized a net investment loss of $3.0 million for the fiscal year ended June 30, 2002 compared with a net investment loss of $2.2 million for the fiscal year ended June 30, 2001. The decreases in investment income are mainly due to the downturn in equity markets.

Deductions from the JRS net assets held in trust for benefits mainly include retirement benefits and administrative expenses. For fiscal year 2002, benefits amounted to $1.6 million, an increase of $135 thousand (9.4 percent) from fiscal year 2001. The increase in benefit payments was due to post retirement benefit increases for benefit recipients. For fiscal year 2002, the costs of administering the plan's benefits amounted to $4 thousand, the same as for fiscal year 2001.

An actuarial valuation of JRS assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 145.60 percent from 153.64 percent at July 1, 2000. The JRS actuarial assets were more than actuarial liabilities by $14.1 million at July 1, 2002, compared with $14.7 million actuarial surplus at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a result of the previous 4-year investment performance.

HPORS

The HPORS provides retirement, disability and death benefits to members of the Montana Highway Patrol. Member and employer contributions, registration fees and earnings on investments fund the benefits of the plan. The HPORS net assets held in trust for benefits at June 30, 2002 amounted to $67.8 million, a decrease of $6.8 million (9.2 percent) from 74.6 million at June 30, 2001.

Additions to the HPORS net assets held in trust for benefits include employer, and member contributions, registration fees and investment income. For the fiscal year ended June 30, 2002, contributions increased from $3.7 million in fiscal year 2001 to $3.8 million, an increase of $79 thousand (2.1 percent). Contributions increased because the number of participating members contributing to the plan increased. Contributions also increased because total compensation reported for active members increased. The plan recognized a net investment loss of $5.6 million for the fiscal year ended June 30, 2002 compared with a net investment loss of $3.8 million for the fiscal year ended June 30, 2001. The decreases in investment income are mainly due to the downturn in equity markets.

Deductions from the HPORS net assets held in trust for benefits mainly include retirement benefits, refunds and administrative expenses. For fiscal year 2002, benefits amounted to $4.9 million, an increase of $237 thousand (5.1 percent) from fiscal year 2001. The increase in benefit payments was due to benefit enhancements enacted by the 2001 Legislature and an increase in benefit recipients. For fiscal year 2002, the costs of administering the plan's benefits amounted to $20 thousand, a decrease of $2 thousand (9.1 percent) from fiscal year 2001.

An actuarial valuation of HPORS assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 86.17 percent from 101.85 percent at July 1, 2000. The HPORS actuarial assets were less than actuarial liabilities by $13.1 million at July 1, 2002, compared with $1.4 million actuarial surplus at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a result of the benefit enhancements enacted by the 2001 Legislature and the previous 4-year investment performance.

FURS

The FURS provides retirement, disability and death benefits to firefighters employed by first and second-class cities and other cities that adopt the plan and firefighters hired by the Montana Air National Guard on or after October 1, 2001. Member, employer, and state contributions and earnings on investments fund the benefits of the plan. The FURS net assets held in trust for benefits at June 30, 2002 amounted to $113.9 million, a decrease of $7.3 million (6.0 percent) from 121.2 million at June 30, 2001.

Additions to the FURS net assets held in trust for benefits include employer, member, and state contributions and investment income. For the fiscal year ended June 30, 2002, contributions increased from $9.5 million in fiscal year 2001 to $10.2 million, an increase of $677 thousand (7.1 percent). Contributions increased because the number of participating members contributing to the plan increased. Contributions also increased because total compensation reported for active members increased. The plan recognized a net investment loss of $8.8 million for the fiscal year ended June 30, 2002 compared

with a net investment loss of $6.0 million for the fiscal year ended June 30, 2001. The decreases in investment income are mainly due to the downturn in equity markets.

Deductions from the FURS net assets held in trust for benefits mainly include retirement benefits, refunds and administrative expenses. For fiscal year 2002, benefits amounted to $8.5 million, an increase of $489 thousand (6.1 percent) from fiscal year 2001. The increase in benefit payments was due to benefit enhancements enacted by the 2001 Legislature and an increase in benefit recipients. For fiscal year 2002, the costs of administering the plan's benefits amounted to $39 thousand, a decrease of $4 thousand (9.3 percent) from fiscal year 2001.

An actuarial valuation of FURS assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 68.9 percent from 76.08 percent at July 1, 2000. The FURS actuarial assets were less than actuarial liabilities by $61.6 million at July 1, 2002, compared with $38.8 million actuarial liability at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a result of the benefit enhancements enacted by the 2001 Legislature and the previous 4-year investment performance.

VFCA

The VFCA provides retirement, disability and death benefits to all volunteer firefighters who are members of eligible volunteer fire companies in unincorporated areas. State contributions and earnings on investments fund the benefits of the plan. The VFCA net assets held in trust for benefits at June 30, 2002 amounted to $16.8 million, a decrease of $919 thousand (5.2 percent) from 17.7 million at June 30, 2001.

Additions to the VFCA net assets held in trust for benefits include state contributions and investment income. For the fiscal year ended June 30, 2002, contributions increased from $1.0 million in fiscal year 2001 to $1.1 million, an increase of $131 thousand (13.1 percent). Contributions increased because there was an increase in the fire insurance premium taxes collected. The plan recognized a net investment loss of $591 thousand for the fiscal year ended June 30, 2002 compared with a net investment loss of $260 thousand for the fiscal year ended June 30, 2001. The decreases in investment income are mainly due to the downturn in equity markets.

Deductions from the VFCA net assets held in trust for benefits mainly include retirement benefits, supplemental insurance payments and administrative expenses. For fiscal year 2002, benefits amounted to $1.4 million, an increase of $529 thousand (60.0 percent) from fiscal year 2001. The increase in benefit payments was due to benefit enhancements enacted by the 2001 Legislature and an increase in benefit recipients. For fiscal year 2002, the costs of administering the plan's benefits amounted to $38 thousand, a decrease of $4 thousand (9.5 percent) from fiscal year 2001.

An actuarial valuation of VFCA assets and benefit obligations is performed every two years. At July 1, 2002, the date of the most recent actuarial valuation, the funded status of the plan decreased to 71.82 percent from 106.07 percent at July 1, 2000. The VFCA actuarial assets were less than actuarial liabilities by $7.6 million at July 1, 2002, compared with $1.0 million actuarial surplus at July 1, 2000. The decrease in funded status as of the last actuarial valuation is a

result of the benefit enhancements enacted by the 2001 Legislature and the previous 4-year investment performance.

Actuarial Valuations and Funding Progress

An actuarial valuation of each of the PERB's defined benefit plans is performed every two years. At the date of the most recent actuarial valuation, July 1, 2002, the funded status of each of the plans is shown in the Schedule of Funding Progress on pages A-56 and A-57.

Funding ratios range from a high of 145.60 percent to a low of 63.27 percent. The table shows the July 1, 2002 funding ratios compared with the ratios at July 1, 2000 and July 1, 1998. The table also shows the amount by which actuarial assets exceeded or fell short of actuarial liabilities. The funding ratio decline is a result of the overall investment performance of prior years and the benefit enhancements granted by the 2001 Legislature. The full impact of investment market downturn during 2000, 2001 and 2002 is not yet reflected in the funding status. At July 1, 2002, the actuarial value of assets exceeded the market value of assets by $611 million compared with a market value of assets exceeding the actuarial value of assets by $489 million at July 1, 2000.

Defined Contribution Plans

The MPERA administers two defined contribution plans; The Public Employees' Retirement System - defined contribution retirement plan (PERS-DCRP) and the Deferred Compensation (457) Plan. On the following page are schedules of Net Assets and Changes in Net Assets for the two defined contribution plans.

PERS-DCRP

The PERS-DCRP is established under Section 401(a) of the Internal Revenue Code. This plan provides retirement benefits for plan members. This plan was available to all active PERS members effective July 1, 2002. The plan member and employer contributions and earnings on investments fund the benefits of the plan.

The PERB has received a long-term loan from the Montana Department of Administration to fund the plan start-up and implementation costs. As of June 30, 2002, the loan balance is $1.5 million. The term of the loan is ten years with interest payments beginning August 15, 2000 and principle payments beginning August 15, 2003. A schedule of the available investment options is available on page A-17.

Deferred Compensation (457) Plan

The Deferred Compensation Plan is established under Section 457 of the Internal Revenue Code. This plan provides supplemental retirement benefits for plan participants. The Deferred Compensation Plan is funded by contributions and by investment earnings. The plan net assets held in trust for benefits at June 30, 2002 amounted to $196.4 million, a decrease of $3.9 million (1.9 percent) under net assets at June 30, 2001.

Additions to the Deferred Compensation Plan net assets held in trust for benefits include contributions and investment income. For fiscal year 2002, contributions increased from those of fiscal year 2001 from $12.3 million to $13.6 million, an increase of $1.3 million (10.8 percent). Contributions increased because of increased participation. The plan recognized a net investment loss of

$4.4 million for fiscal year 2002 compared with a net investment loss of $3.0 million for fiscal year 2001. The negative return from investments was mainly due to a downturn in the equity markets.

Deductions from the Deferred Compensation Plan net assets mainly include member and beneficiary refunds, miscellaneous expenses and administrative expenses. For fiscal year 2002, refunds amounted to $11.5 million, an increase of $4.4 million (61.4 percent) over fiscal year 2001. The increase in refunds was due to an increase in withdrawals for fiscal year 2002.

Benefit obligations of the Deferred Compensation Plan are equal to the member account balances, which are equal to net assets of the plan. A schedule of the available investment options is on page A-17.

Net Assets - Defined Contribution Plans

As of June 30, 2002 - and comparitive totals for June 30, 2001

(dollars in thousands)

	PERS-DCRP		457-PLAN		TOTAL		Total %
	2002	2001	2002	2001	2002	2001	Change
Assets:							
Cash and Receivables	535	147	2,358	4,421	2,893	4,568	-36.7%
Securities Lending Collateral				7,229	0	7,229	-100.0%
Investments			194,201	196,443	194,201	196,443	-1.1%
Total Assets	535	147	196,559	208,093	197,094	208,240	-5.4%
Liabilities:							
Secuity Lending Collateral				7,229	0	7,229	-100.0%
Other Payables	1,562	732	139	584	1,701	1,316	29.3%
Total Liabilities	1,562	732	139	7,813	1,701	8,545	-80.1%
Total Net Assets	(1,027)	(585)	196,420	200,280	195,393	199,695	-2.2%

Changes In Net Assets - Defined Contribution Plans

For the year ended June 30, 2002 - and comparative totals for June 30, 2001

(dollars in thousands)

	PERS-DCRP		457-PLAN		TOTAL		Total %
	2002	2001	2002	2001	2002	2001	Change
Additions:							
Contributions			13,583	12,264	13,583	12,264	10.8%
Investment Income (Loss)	3	4	(4,434)	(2,962)	(4,431)	(2,958)	49.8%
Total Additions	3	4	9,149	9,302	9,152	9,306	-1.7%
Deductions:							
Refunds			11,460	7,102	11,460	7,102	61.4%
Administrative Expenses	445	270	242	175	687	445	54.4%
Miscellaneous Expenses			811	971	811	971	-16.5%
Prior Period Adjustment		(15)	496	76	496	61	713.1%
Total Deductions	445	255	13,009	8,324	13,454	8,579	56.8%
Increase(decrease) in net assets	(442)	(251)	(3,860)	978	(4,302)	727	-691.7%

Defined Contribution Plans
Investment Options

PERS-DCRP

International Stock Funds
- American Funds New Perspective
- SSGA International Growth Opportunities

Small Company Stock Funds
- Brown Capital Small Co Instl
- SEI Instl Mgd Small Cap Value A
- Vanguard Small Cap Index Adm

Mid-Sized Company Stock Funds
- Artisan Mid Cap
- MSIF Trust Mid Cap Value - Inst

Large Company Stock Funds
- American Funds Growth Fund A
- Vanguard Equity-Income Adm
- Vanguard Growth & Income Adm

Balanced Funds
- Vanguard Balanced Index

Bond Funds
- N/A

Fixed Investment Options
- DCRP Fixed Fund

Profile Funds
- N/A

Deferred Compensation (457) Plan

International Stock Funds
- Artisan International
- Janus Worldwide
- Mutual Discovery Z
- Templeton Foreign A

Small Company Stock Funds
- Neuberger Berman Genesis
- RS Diversified Growth

Mid-Sized Company Stock Funds
- Franklin Small-Mid Cap Growth
- Janus Enterprise
- Strong Opportunity Inv

Large Company Stock Funds
- Davis NY Venture A
- Dreyfus Premier Third Cent Z
- Fidelity Contrafund
- Fidelity Equity-Income
- Fidelity Growth & Income
- Fidelity Magellan
- Putnam Investors
- TCW Galileo Select Equities N
- Vanguard 500 Index

Balanced Funds
- Dodge & Cox Balanced
- Janus Balanced

Bond Funds
- Columbia High-Yield
- PIMCO Total Return Admin

Fixed Investment Options
- Montana Fixed Fund

Profile Funds
- Aggressive
- Moderately Aggressive
- Moderate
- Moderately Conservative
- Conservative

Public Employees' Retirement Board

A Component Unit of the State of Montana

Combined Statement of Fiduciary Net Assets - Pension Trust Funds

as of June 30, 2002

	PERS DBRP	PERS EDUCATION	MPORS	GWPORS	SRS	JRS
Assets						
Cash and Short-term Investments	$ 65,704,766	727,780	1,569,616	1,876,430	3,371,454	1,036,819
Securities Lending Collateral (Note A3)	127,172,568		6,460,433	1,757,068	6,416,946	2,067,494
Receivables						
Interest	12,405,440		548,954	149,019	547,093	177,578
Accounts Receivable	5,146,304		384,105		371,650	
Due from other funds	696,772	68,146		8,035		
Due from Primary Gov't	32,401		6,529,108			
Notes Receivable	438,528				58,445	
Total Receivables	18,719,445	68,146	7,462,167	157,054	977,188	177,578
Investments, at fair value (Note A3)						
Montana Stock Pool (MTCP)	946,374,506		42,820,488	11,576,493	43,177,900	14,012,217
Retirement Fund Bond Pool (RFBP)	858,466,949		46,044,780	12,657,553	45,736,435	14,877,545
Montana International Pool (MTIP)	215,598,191		9,694,650	2,555,052	9,593,057	2,995,415
Montana Private Equity Pool (MPEP)	95,926,866		4,167,039	1,114,798	4,167,040	1,353,151
Equity Index Fund	192,492,844		8,271,457	2,585,689	8,875,473	2,900,315
Real Estate Investments	7,035,303					
Mortgages & Commercial Loans net of Accumulated Mortgage Discount	178,441,866					
Deferred Comp Fixed Investments						
Deferred Comp Variable Investments						
Deferred Comp Life Insurance						
Total Investments	2,494,336,525		110,998,414	30,489,585	111,549,905	36,138,643
Property and Equipment, at cost, net of accumulated depreciation (Note A2)	2,359					
Total Assets	2,705,935,663	795,926	126,490,630	34,280,137	122,315,493	39,420,534
Liabilities						
Securities Lending Collateral Liability	127,172,568		6,460,433	1,757,068	6,416,946	2,067,494
Accounts Payable	13,908,785	18,101	290	35,098	390,676	
Due to other funds	69,117	3,718	49,307	29,883	39,915	4,268
Due to Primary Gov't	45,887					
Notes Payable (Note C)						
Deferred Revenue	13,537		570	2,458	78	
Compensated Absences	226,296	5,411				
Total Liabilities	141,436,190	27,230	6,510,600	1,824,507	6,847,615	2,071,762
Net Assets Held in Trust for Pension Benefits (see schedule of funding progress, page A-56)	$ 2,564,499,473	768,696	119,980,030	32,455,630	115,467,878	37,348,772

The notes to the financial statements are an integral part of this statement.

		Defined Benefit Pension Plans		Defined Contribution Plans			
			Total Defined Benefit Pension Plans	PERS		Total Defined Contribution Plans	Total Pension Trust Funds
HPORS	FURS	VFCA		DCRP	457 Plan		2002
833,376	1,351,136	1,811,717	78,283,094	534,537	2,305,251	2,839,788	81,122,882
3,800,253	6,162,703	1,011,614	154,849,079				154,849,079
324,730	520,678	86,159	14,759,651				14,759,651
	293,815		6,195,874				6,195,874
631			773,584	1,186	51,955	53,141	826,725
58,100	5,764,368		12,383,977				12,383,977
			496,973				496,973
383,461	6,578,861	86,159	34,610,059	1,186	51,955	53,141	34,663,200
25,562,750	40,946,051	4,099,639	1,128,570,044				1,128,570,044
27,229,863	43,774,563	7,837,559	1,056,625,247				1,056,625,247
5,590,386	9,336,569	1,262,163	256,625,483				256,625,483
2,467,949	3,928,688	627,885	113,753,416				113,753,416
5,729,295	8,001,836	1,193,676	230,050,585				230,050,585
			7,035,303				7,035,303
			178,441,866				178,441,866
					122,729,210	122,729,210	122,729,210
					71,459,943	71,459,943	71,459,943
					12,316	12,316	12,316
66,580,243	105,987,707	15,020,922	2,971,101,944		194,201,469	194,201,469	3,165,303,413
			2,359				2,359
71,597,333	120,080,407	17,930,412	3,238,846,535	535,723	196,558,675	197,094,398	3,435,940,933
3,800,253	6,162,703	1,011,614	154,849,079				154,849,079
			14,352,950	41,326	111,973	153,299	14,506,249
19,851	39,488	38,208	293,755	14,552	5,801	20,353	314,108
		95,170	141,057				141,057
				1,498,000		1,498,000	1,498,000
	3,404		20,047				20,047
			231,707	8,593	20,793	29,386	261,093
3,820,104	6,205,595	1,144,992	169,888,595	1,562,471	138,567	1,701,038	171,589,633
67,777,229	113,874,812	16,785,420	3,068,957,940	(1,026,748)	196,420,108	195,393,360	3,264,351,300

Public Employees' Retirement Board

A Component Unit of the State of Montana

Combined Statement of Changes in Fiduciary Net Assets- Pension Trust Funds

for the Fiscal Year Ended June 30, 2002

	PERS					
	DBRP	EDUCATION	MPORS	GWPORS	SRS	JRS
Additions						
Contributions (Note D)						
Employer	$ 55,548,285		3,272,651	1,594,926	2,387,118	1,032,319
Plan Member	59,938,131		2,164,076	1,825,262	2,456,283	279,977
Membership Fees	167					
Interest Reserve Buyback	92,341		7,214	21,292	40,463	
Retirement Incentive Program	144,782				44,180	
Registration Fee Collections						
Miscellaneous Revenue	459	137				
Education Contributions		812,277				
State Contribution	373,721		6,529,108			
Total Contributions	116,097,886	812,414	11,973,049	3,441,480	4,928,044	1,312,296
Investment Income (Note A3)						
Net Appreciation (Depreciation)						
in Fair Value of Investments	(309,265,747)		(13,821,700)	(3,791,568)	(13,758,381)	(4,649,969)
Interest	96,913,351	34,831	4,058,221	1,078,637	4,056,264	1,431,296
Dividends	14,248,194		642,956	174,572	650,178	212,578
Securities Gain (Loss)						
Securities Lending Income	3,515,060	628	177,805	47,587	177,028	57,014
	(194,589,142)	35,459	(8,942,718)	(2,490,772)	(8,874,911)	(2,949,081)
Less:						
Investment Expense	3,784,820		123,484	32,431	123,497	48,184
Securities Lending Rebate and Fees	3,026,454	562	153,826	41,170	153,151	49,341
	6,811,274	562	277,310	73,601	276,648	97,525
Net Investment Income	(201,400,416)	34,897	(9,220,028)	(2,564,373)	(9,151,559)	(3,046,606)
Total Additions	(85,302,530)	847,311	2,753,021	877,107	(4,223,515)	(1,734,310)
Deductions (Note D)						
Benefits	114,662,817		9,844,541	1,230,427	3,699,727	1,566,110
Refund of Member Contributions	10,683,442		344,854	316,677	409,065	
Refunds to Other Plans	364,421		3,607	14,094	37,501	
Supplemental Insurance Payments						
Administrative Expense	1,824,937	1,485,230	49,307	29,883	39,915	4,269
Miscellaneous Expenses						
Total Deductions	127,535,617	1,485,230	10,242,309	1,591,081	4,186,208	1,570,379
Net Increase (Decrease)	(212,838,147)	(637,919)	(7,489,288)	(713,974)	(8,409,723)	(3,304,689)
Net Assets Held in Trust for Pension Benefits						
Beginning of Year (*restated for 457*)	2,777,337,620	1,406,615	127,469,318	33,169,604	123,877,601	40,653,461
Prior Period Adjustment						
End of Year	2,564,499,473	768,696	119,980,030	32,455,630	115,467,878	37,348,772

The notes to the financial statements are an integral part of this statement.

		Defined Benefit Pension Plans		Defined Contribution Plans			
			Total Defined Benefit	PERS		Total Defined Contribution	Total Pension Trust Funds
HPORS	FURS	VFCA	Pension Plans	DCRP	457 Plan	Plans	2002
2,769,841	2,521,295		69,126,435		46,412	46,412	69,172,847
693,000	1,871,837		69,228,566		13,313,925	13,313,925	82,542,491
			167			-	167
	2,468		163,778			-	163,778
			188,962			-	188,962
308,973			308,973			-	308,973
			596	178	222,615	222,793	223,389
			812,277			-	812,277
	5,764,368	1,133,741	13,800,938			-	13,800,938
3,771,814	10,159,968	1,133,741	153,630,692	178	13,582,952	13,583,130	167,213,822
(8,618,003)	(13,207,870)	(1,341,064)	(368,454,302)		(13,905,751)	(13,905,751)	(382,360,053)
2,706,223	3,834,101	706,673	114,819,597	3,173	9,035,503	9,038,676	123,858,273
388,777	614,502	61,076	16,992,833				16,992,833
			-		676,639	676,639	676,639
104,630	169,581	28,969	4,278,302	57	106,837	106,894	4,385,196
(5,418,373)	(8,589,686)	(544,346)	(232,363,570)	3,230	(4,086,772)	(4,083,542)	(236,447,112)
80,681	108,640	21,637	4,323,374		252,435	252,435	4,575,809
90,527	146,652	25,258	3,686,941	51	94,876	94,927	3,781,868
171,208	255,292	46,895	8,010,315	51	347,311	347,362	8,357,677
(5,589,581)	(8,844,978)	(591,241)	(240,373,885)	3,179	(4,434,083)	(4,430,904)	(244,804,789)
(1,817,767)	1,314,990	542,500	(86,743,193)	3,357	9,148,869	9,152,226	(77,590,967)
4,861,329	8,507,526	1,410,768	145,783,245				145,783,245
130,047	80,454		11,964,539		11,459,674	11,459,674	23,424,213
18,985			438,608				438,608
		12,675	12,675				12,675
19,851	39,488	38,208	3,531,088	445,098	242,211	687,309	4,218,397
					810,882	810,882	810,882
5,030,212	8,627,468	1,461,651	161,730,155	445,098	12,512,767	12,957,865	174,688,020
(6,847,979)	(7,312,478)	(919,151)	(248,473,348)	(441,741)	(3,363,898)	(3,805,639)	(252,278,987)
74,625,208	121,187,290	17,704,571	3,317,431,288	(585,007)	200,280,113	199,695,106	3,517,126,394
					(496,107)	(496,107)	(496,107)
67,777,229	113,874,812	16,785,420	3,068,957,940	(1,026,748)	196,420,108	195,393,360	3,264,351,300

Public Employees' Retirement Board

A Component Unit of the State of Montana

Notes to the Financial Statements

for the Fiscal Years Ended June 30, 2002 and 2001

The Public Employees' Retirement Board (PERB) administers ten retirement plans and the related member education. The retirement plans are eight defined benefit plans and two defined contribution plans. The *defined benefit* retirement plans are the Public Employees' Retirement System (PERS-DBRP), Municipal Police Officers' Retirement System (MPORS), Game Wardens' and Peace Officers' Retirement System (GWPORS), Sheriffs' Retirement System (SRS), Judges' Retirement System (JRS), Highway Patrol Officers' Retirement System (HPORS), Firefighters' Unified Retirement System (FURS), and the Volunteer Firefighters' Compensation Act (VFCA). The *defined contribution* retirement plans are the Public Employees' Retirement System (PERS-DCRP) and the Deferred Compensation (IRC § 457) Plan. The PERS-DCRP was implemented as of July 1, 2002, and available only to eligible members of the PERS. The Deferred Compensation Plan is available to employees of the state, university and local subdivisions that contract with the plan.

The member education is the means by which the PERS members will be provided the necessary tools to decide between participation in the Defined Benefit Retirement Plan (PERS-DBRP) or the Defined Contribution Retirement Plan (PERS-DCRP). Since eligible defined benefit members have the option of joining the defined contribution plan, the education of the defined benefit plan members has been ongoing since the fall of 2001. The choice is a one-time irrevocable election. With the implementation of the defined contribution plan, education must also begin for the members that choose the defined contribution plan. This education will include information on investment choices and will begin when members transfer into the plan. For this reason, the MPERA established a defined contribution education fund as of July 1, 2002.

The assets of each plan are maintained separately, including member education, and may be used only for the payment of benefits to the members of the respective plan and to pay administrative expenses of the respective plan, in accordance with the terms of each plan as prescribed in Title 19, of the Montana Code Annotated (MCA).

A. Summary of Significant Accounting Policies

1. Basis of Accounting

The PERB is a discretely presented component unit Pension Trust Fund of the State of Montana financial reporting entity. The Montana Public Employee Retirement Administration (MPERA), staff of the PERB, prepares the accounting records and financial statements for the fiduciary/pension trust funds using the accrual basis of accounting. For the pension trust funds, member contributions are recognized in the period in which contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Revenues are rec-

ognized in the accounting period in which they are earned and become measurable. Benefits and refunds are recognized in the accounting period in which they are due and payable. Expenses are recognized in the period incurred. Administrative expenses are financed through investment earnings on the pension trust fund in each plan. Interfund receivables and payables exist at year-end because all administrative expenses are accounted for within PERS and then distributed to the other plans at year-end. Participants of the deferred compensation (457) plan are charged fees based on individual account balances. The vendor withholds fees and after payment of the vendor's contractual expenses, the excess fees are submitted to the PERB. The excess fees, recorded as *Miscellaneous Revenue* in the financial statements, are used to pay the Board's deferred compensation related administrative expenses.

Due to the implementation of GASB 34, a fiscal year 2001 comparative total column is not included in the fiscal year 2002 financial statements. Also, the deferred compensation plan was changed from an expendable trust fund (modified accrual) to a pension trust fund (full accrual) in fiscal year 2002. The change in the basis of accounting resulted in a restatement of the fiscal year 2001 *Total Fund Balance* for the deferred compensation plan. In the current fiscal year it is restated as *Net Assets Held In Trust for Pension Benefits Beginning of Year.*

The prior period adjustment for the deferred compensation plan is an adjustment to the fixed investment in the amount of $496,107. This adjustment is regarding an amount listed on the vendor statements as Total Accruals. Initially, the MPERA was informed that Total Accruals were assets that the vendor held on behalf of the plan. Ongoing discussions with the vendor's representatives provided information that Total Accruals, as listed on the statement, was not a valid receivable. The new information required an adjustment to the prior year balance.

2. Property and Equipment Used in Operations

Equipment, valued at $5,000 or more, is recorded at cost less straight-line depreciation over the estimated useful life of five to ten years. Equipment under $5,000 is expensed in the year purchased.

3. Method Used to Value Investments

Defined benefit retirement plan assets are invested on behalf of the plans and managed by the Montana Board of Investments (BOI), Department of Commerce. Investments are purchased in accordance with the statutorily and constitutionally mandated "prudent expert principle." Investments are reported at fair value. As of June 30, 2002, there were five major diversified pools, one more than in fiscal year 2001, Montana Short Term Investment Pool (STIP), Montana Stock Pool (MTCP), Retirement Funds Bond Pool (RFBP), Montana International Pool (MTIP) and Montana Private Equity Pool (MPEP). The MPEP, effective May 1, 2002, allows retirement funds to participate in the venture capital and leveraged buyout markets and other private equity investments via a diversified pool.

The deferred compensation plan's fixed assets were invested and managed on behalf of the plan by State Street Research/ Wells Fargo (SSR/WF) through Decem-

ber 28, 2001 and the BOI through January 7, 2002. The assets managed by the BOI for the deferred compensation plan were invested in STIP and the Trust Fund Bond Pool (TFBP). As of the previous dates, the fixed investments were transferred to the plans new fixed asset manager, Pacific Investment Management Company (PIMCO). The third party record keeper, Great West Life & Annuity Insurance Co., tracks and reports the daily trading and valuations of all investment options including the assets held by the individual mutual fund companies. Investments are reported at fair value as of June 30, 2002.

The following are PERB summaries of the BOI's fiscal year end statements, the SSR/WF contract, the PIMCO contract and a statement about the variable investments.

STIP portfolio includes asset-backed securities, variable-rate (floating-rate) instruments and covered options. These securities provide a diversified portfolio earning a competitive total rate of return. Funds may be invested for relatively short periods. State agencies are legally required to invest in STIP and the PERB elects to have all STIP income automatically reinvested. Investments are reported at fair value based on market prices supplied to the BOI by various pricing services. The unit value is fixed at $1.00. A purchased unit earns income on the purchase date and ceases to earn income on the day before the unit is sold. STIP income reflects the monthly earnings of the STIP portfolio and is distributed on the first calendar day of the month with the exception of the June distribution. Income for June is distributed on the last calendar day of the month. Administrative expenses incurred by the BOI are charged daily to STIP based on their expenses applicable to STIP. STIP investments are required to have the highest rating in the short term category by any Nationally Recognized Statistical Rating Organization. STIP is considered an external investment pool per the Governmental Accounting Standards Board (GASB) Statement No. 31 and is classified as a "2a7-like" pool. STIP is not registered with the Securities and Exchange Commission (SEC) but does operate in a manner consistent with SEC rules. *Disclosure about Derivatives:* STIP holds two types of securities that are required to be disclosed per the GASB. 1) Asset-backed securities are collateralized by a pool of mortgage and non-mortgage assets pledged by the issuer. 2) Variable-rate (floating-rate) securities are sensitive to interest rate changes. There are no legal risks that the BOI is aware of regarding any STIP investments.

MTCP portfolio includes common stock, convertible equity securities and equity derivatives. In June 2000, the BOI approved a staff recommendation to securitize cash by investing in an equity derivative, the State Street Stock Performance Index Futures Fund (SPIFF). Portfolio cash is swept daily into SPIFF maintaining 100% equity exposure through holdings of stock index futures. MTCP is carried at fair value for financial reporting purposes. The value of units purchased by participants increased $7,200,000 in fiscal year 2002. The $82,000,000 in participant purchases in fiscal year 2002 reflect investment opportunities given the market conditions. Equity investments, traded on a national security exchange, are stated at the last-reported sales price on valuation day. Security transactions are recorded as

of trade date rather than settlement date; therefore, the MTCP portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received. The unit values are calculated daily. MTCP income available for distribution is distributed on the first business day of each month. Units are bought/sold upon the decision of the BOI's Investment Officer.

The BOI received a summons and complaint, dated October 11, 2002, regarding the bankruptcy of Owens-Corning. The company seeks a determination that the dividend payments from October 1996 through July 2000 represent "fraudulent transfers under Chapter 11 Bankruptcy provisions and applicable state law, and are, therefore, voidable". The complaint states the Montana Board of Investments was the "recipient of dividends in the amount of $357,099 for the relevant period".

RFBP portfolio includes corporate asset-backed, other corporate, U.S. government mortgage-backed, U.S. government and Yankee securities. RFBP investments are presented at fair value. Fair values are determined, primarily, by reference to fair prices supplied to the BOI by its custodial bank, State Street Bank and Trust. Premiums and discounts are amortized/accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Unit values are calculated weekly and at month end, based on portfolio pricing, to allow for participant transactions to occur as determined by the BOI's Investment Officer. The June 30, 2002 unit value of $103.56 increased from the June 30, 2001 unit value of $102.04. Interest rates declined during the fiscal year, which has the effect of increasing bond prices and the pool unit value. Accumulated income is distributed monthly on the first calendar day of the month. Realized portfolio gains/losses are distributed at least annually. *Disclosure about Derivatives*: The RFBP portfolio includes structured financial instruments known as REMICs (Real Estate Mortgage Investment Conduits). These securities are required to be disclosed per the GASB. REMICs are pass-through vehicles for multiclass mortgage-backed securities. Some REMICs are principal-only strips (POs) and interest-only strips (IOs).

As of June 30, 2002, Burlingon Industries, Inc., Enron Corp. and WorldCom Inc. presented legal and higher credit risks to the BOI. The RFBP holds a Burlington Industries, Inc., $6,000,000 par, 7.25% bond maturing September 15, 2005. In September 2000, the company announced a reduction of stockholders equity. Due to an increasing senior bank line and declining credit trend, the bond ratings for this issue were downgraded, in May 2001, by the Moody's and Standard and Poor's rating agencies. During fiscal year 2001, the book value of Burlington Industries, Inc. was reduced to $2,400,000. Due to the company's filing for Chapter 11 bankruptcy protection on November 11, 2001, the book value was reduced to $1,200,000. The company is expected to emerge from bankruptcy in 2003. The RFBP holds a $7,000,000 par 6.40% Enron bond maturing July 15, 2006 and a $7,000,000 par 6.95% Enron bond maturing July 15, 2028. The combined book value of theses securities was $13,582,030 as of November 30, 2001. Enron Corp. filed for Chapter 11 bankruptcy protection on December 12, 2001.

Accordingly, the book value was reduced for the two issues from $14,000,000 to $5,600,000 as of June 30, 2002. In October 2002, the book value was reduced to $2,800,000 for both issues. The BOI, currently, anticipates receiving up to $2,800,000 from bankruptcy claims. The RFBP portfolio includes a $6,000,000 par 6.95% WorldCom Inc. bond maturing August 15, 2028. The book value of this bond, originally purchased at a discount, was $5,477,400 on June 30, 2002. On July 21, 2002 WorldCom Inc. filed for Chapter 11 bankruptcy protection. As of July 31, 2002, the reduced book value is $2,400,000. At this time, the BOI expects bankruptcy recovery up to $2,400,000. On November 7, 2002, the Attorney General for the State of Montana filed a lawsuit against certain Worldcom executives, directors and financial institutions associated with Worldcom such as Arthur Andersen and CitiGroup. The lawsuit, filed in Lewis and Clark County, Montana, alleges that the defendants filed "false and misleading registration statements" relating to the purchase of the bonds by the Montana Board of Investments.

As of June 30, 2001, the Rite Aid Corporation, Asarco Inc. and Service Corp. presented a higher credit risk to the BOI. The RFBP holds a $7,000,000 par, 7.13% Rite Aid bond maturing January 15, 2007. In May 2000, the BOI was subordinated to a secured bank line of credit on this issue and the bond ratings were downgraded by the Moody's and the Standard & Poor's bond ratings agencies. Based on this subordination and ratings downgrade, the BOI reduced the book value to $5,600,000 as of June 30, 2000. During fiscal year 2001, the book value was further reduced to $5,220,172. Due to an improving credit trend, amortization was resumed in June 2001. The book value of the Rite Aid security at June 30, 2002 is $5,541,139. As of June 30, 2002, Rite Aid does not represent a credit risk. The RFBP held a $7,000,000 par, 7.875% Asarco Inc. bond maturing April 15, 2013. Due to bond rating downgrades, high leverage and increased production costs, the book value of this security was reduced to $5,600,000 as of June 30, 2001. In February 2002, the book value of this security was further reduced to $4,200,000. In May 2002, this bond was sold, on the market, for $3,474,250 including interest. The RFBP holds two issues of Service Corp. These issues include a $5,000,000 par, 6.875% bond maturing October 1, 2007, and a $5,000,000 par 6% bond maturing December 15, 2005. In January 2001, the bond ratings for these two issues were downgraded by the Moody's rating agency. The book value of these two issues is $4,000,000 each as of June 30, 2002 and 2001. Due to an improved credit outlook, Service Corp. is not considered a credit risk as of June 30, 2002.

The BOI received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, $5,000,000 par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002 sale of the bond at a price of $94.669 plus accrued interest. Deutsche Bank Securities seeks damages of $538,632 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. The BOI tendered the Pennzoil Quaker State hold-

ings on October 8, 2002 at a price of $113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, the Board received $5,683,075 in principal and interest plus $150,000 as a consent fee.

MTIP portfolio includes equity investments in four funds – BOI's Internal International, and three externally managed funds: Pyrford International, Schroder Investment Management NA, and SG Pacific Asset Management Inc. The four funds invest in securities of foreign-based corporations listed on legal and recognized foreign exchanges as well as domestic exchanges. Investments are presented at current U.S. dollar after conversion from foreign currency by the custodial bank, State Street Bank and Trust. Unit values are calculated weekly and once a month at the close of the last business day of the month, based on fair value of MTIP equity holding, other assets and liabilities. Based on the BOI Investment Officer's decision, participants are allowed to buy or sell units on the first business day of each month. Realized gains/losses from the sale of securities and related foreign exchange transactions are retained by the fund. MTIP income is distributed at least quarterly to the retirement fund, net of external manager fees and administrative expenses, on the first business day of the following month. As of June 30, 2002 and 2001, the BOI was unaware of any legal, market or credit risks regarding the MTIP investments.

MPEP portfolio includes venture capital, leveraged buyout, mezzanine, special situation and secondary investments. The MPEP was established in April 2002 to allow retirement funds the opportunity to participate in the venture capital and leveraged buyout markets and other private equity investments via a diversified pool. The BOI chose to securitize MPEP cash by investing in an equity derivative, the State Street Stock Performance Index Futures Fund (SPIFF). Given the complexity and specialization of private equity investment, the BOI contracts with five private equity managers. The private equity managers include Adams Street Partners (formerly Brinson Partners); Kohlberg, Kravis, Roberts and Company (KKR); Welsh Carson Anderson and Stowe; Madison Dearborn Partners; and Lexington Partners. Investments are presented at fair value and because no recognized market exists for private equity investment, the investments, on valuation date, are stated at the fair value reported in the most recent external managers' valuation reports. Carrying value represents the private equity security purchase price. MPEP security transactions are recorded as of trade date rather than settlement date; therefore, the MPEP portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received. Unit values are calculated at month end and participant transactions will most likely occur on a quarterly basis. Based on the BOI Investment Officer's decision, participants are allowed to buy, reinvest or sell units on the first business day of each month. MPEP does not participate in security lending. Portfolio diversification of risk is to be achieved through multiple partnership relationships and investments. Private equity investments are recognized as investments with a higher degree of risk with a higher return potential, whereas, private equity investments typically have a low correlation and should contribute to reduction of portfolio risk.

Other Investments include venture capital, leveraged buy-outs, equity index, real estate, mortgages and loans. Effective May 1, 2002, all the venture capital and leveraged buyout investments totaling $159,799,310, at cost, were transferred to the new Montana Private Equity Pool (MPEP) along with $15 million in cash. Venture capital represents private equity investments in early-stage financing of rapidly growing companies with an innovative product or service. Leveraged buyouts permit investment groups to acquire a company by leveraging debt, as a financing technique, to establish a significant ownership position on behalf of the company's current management team. Equity index investments are investments in selected mutual funds whose equity portfolios match a broad based index or composite. Real estate investments held, in part, for the PERS include the IBM building at 100 North Park Avenue in Helena, MT; a three-story building at 2401 Colonial Drive in Helena, MT; property located on California Street in Helena, MT; and an office building to be constructed in Bozeman, MT. The BOI also holds the building located at 1712 Ninth Avenue in Helena, MT for the sole benefit of the PERS. The real estate investments and residential and multi-family mortgages are valued based on a discounted cash flow. Premiums and discounts are amortized/accreted using the straight-line or interest method to the call, average life or maturity date of the securities. All other investments are presented at fair value. Fair values are determined, primarily, by reference to fair value prices supplied to the BOI by its custodial bank, State Street Bank and Trust. As of June 30, 2002 and 2001, there were no uncollectible account balances for Montana mortgages and loans receivable; however, during fiscal year 2002, the BOI staff wrote off loan principal balances in the total amount of $1,794,968. In fiscal year 2002, the sale of pool units from the MTCP, TFBP, and RFBP generated a net gain to participants of $14 million.

Securities Lending, governed under the provisions of state statutes, authorizes the custodial bank, State Street Bank and Trust, to lend the BOI's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. This is accomplished by the BOI via a Securities Lending Authorization Agreement. During the period the securities are on loan, the BOI receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the fair value of the loaned security and maintain collateral equal to not less than 100 percent of the fair value of the loaned security. The BOI retains all rights and risks of ownership during the loan period. During fiscal years 2002 and 2001, State Street Bank and Trust lent, on behalf of the BOI, certain securities held by State Street Bank and Trust, as custodian, and received U.S. dollar currency cash, U.S. government securities, and irrevocable bank letters of credit. State Street Bank and Trust does not have the ability to pledge or sell collateral securities unless the borrower defaults. The BOI did not impose any restrictions during fiscal year 2002 and 2001 on the amount of the loans that State Street Bank and Trust made on its behalf. There were no failures by any borrowers to return loaned securities or pay distributions thereon during fiscal years 2002 and 2001. Moreover, there were no losses during fiscal years 2002 and 2001 resulting from a default of the borrowers or State Street. During fiscal

years 2002 and 2001, the BOI and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the BOI's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the BOI could not determine. On June 30, 2002 and June 30, 2001, the BOI had no credit risk exposure to borrowers.

TFBP portfolio includes corporate asset-backed, other corporate, U.S. government mortgage-backed, U.S. government, Yankee securities and cash investments. In January 2002, the State of Montana Section 457 Deferred Compensation Plan withdrew all funds from the TFBP due to a new contract with another investment manager. TFBP investments are presented at fair value. Fair values for securities are determined primarily by reference to market prices supplied to the BOI by it's custodial bank, State Street Bank and Trust. Premiums and discounts are amortized/ accreted using the straight-line or scientific method to the call, average life or maturity date of the securities. Unit values are calculated weekly and at month end, based on portfolio pricing, to allow for participant transactions to occur as determined by the BOI Investment Officer. The June 30, 2002 unit value of $98.61 increased from a June 30, 2001 unit value of $97.18. Security transactions are recorded as of trade date rather than settlement date; therefore, the TFBP portfolio at June 30 may include receivables from brokers for securities sold but not delivered, and payables to brokers for securities purchased but not received. Accumulated income is distributed monthly on the first calendar day of each month. Realized portfolio gains/losses are distributed at least annually to the participants. *Disclosure about Derivatives*: The TFBP includes structured financial instruments known as REMICs (Real Estate Mortgage Investment Conduits). The GASB requires these securities to be disclosed. REMICs are pass-through vehicles for multiclass mortgage-backed securities. Some REMICs are principal-only strips (POs).

As of June 30, 2002, Enron Corp., Burlington Industries, Inc. and WorldCom Inc. presented legal and higher credit risks to the BOI. The TFBP holds a $2,000,000 par, 6.75% Enron bond maturing August 1, 2009, a $3,000,000 par 6.40% Enron bond maturing July 15, 2006 and a $3,000,000 par 6.95% Enron bond maturing July 15, 2028. The combined book value of these securities was $7,560,870 as of November 30, 2001. Enron Corp. filed for Chapter 11 bankruptcy protection on December 12, 2001. Accordingly, the BOI reduced the book value for the three issues to $3,200,000 as of June 30, 2002. In October 2002, the book value was reduced to $1,600,000 for the three issues. The BOI, currently, anticipates receiving up to $1,600,000 from bankruptcy claims. The TFBP holds a Burlington Industries, Inc., $4,000,000 par, 7.25% bond maturing September 15, 2005. In September 2000, the company announced a reduction of stockholders' equity. Due to an increasing senior bank line and declining credit trend, the bond ratings for this issue were downgraded, in

May 2001, by the Moody's and Standard and Poor's rating agencies. During fiscal year 2001, the book value of Burlington Industries Inc. was reduced to $1,600,000. Due to the company's filing for Chapter 11 bankruptcy protection on November 11, 2001, the book value was reduced to $800,000. The company is expected to emerge from bankruptcy in 2003. The TFBP portfolio also includes a $9,000,000 par 6.95% WorldCom Inc. bond maturing August 15, 2028. The book value of this bond, originally purchased at a discount, was $8,216,000 on June 30, 2002. On July 21, 2002 WorldCom Inc. filed for Chapter 11 bankruptcy protection. As of July 31, 2002, the reduced book value is $3,600,000. At this time, the BOI expects bankruptcy recovery up to $3,600,000. On November 7, 2002, the Attorney General for the State of Montana filed a lawsuit against certain Worldcom executives, directors and financial institutions associated with Worldcom such as Arthur Andersen and CitiGroup. The lawsuit, filed in Lewis and Clark County, Montana, alleges that the defendants filed "false and misleading registration statements" relating to the purchase of the bonds by the Montana Board of Investments.

The TFBP holds a $5,000,000 par, 7.875% Asarco Inc. bond maturing April 15, 2013. Due to bond rating downgrades, high leverage and increased production costs, the book value of this security was reduced to $4,000,000 as of June 30, 2001. In February 2002, the book value of this security was further reduced to $3,000,000. In May 2002, this bond was sold, on the market, for $2,478,719 including interest. The BOI owns a Rite Aid $3,000,000 par, 7.13% bond maturing January 15, 2007. In May 2000, the BOI was subordinated to a secured bank line of credit on this issue and the bond ratings were downgraded by the Moody's and Standard & Poor's bond ratings agencies. Based on this subordination and ratings downgrade, the book value was reduced to $2,400,000 as of June 30, 2000. During fiscal year 2001, the book value was further reduced to $1,800,000. Due to an improving credit trend, amortization was resumed in June 2001. The book value of this security at June 30, 2002 is $2,374,356. As of June 30, 2002, Rite Aid does not represent a credit risk. The TFBP holds a Service Corp. $5,000,000 par 6% bond maturing December 15, 2005. In January 2001, the bond rating for this issue was downgraded by the Moody's bond rating agency. As of June 30, 2002 and 2001, the book value of this issue is $4,000,000. Due to improved credit outlook, Service Corp. is not considered a credit risk as of June 30, 2002.

The BOI received a summons and complaint, dated September 3, 2002, regarding the sale of a Pennzoil Quaker State, $8,000,000 par, 6.75% corporate bond maturing April 1, 2009. Deutsche Bank Securities claims a "breach of contract" for the March 25, 2002 sale of the bond at a price of $94.669 plus accrued interest. Deutsche Bank Securities seeks damages of $861,811 for the additional costs incurred to acquire the bond from third parties, plus any statutory interest, costs and expenses. On October 1, 2002, Shell Oil Company acquired Pennzoil and subsequently announced a public tender of Pennzoil Quaker State debt. The BOI tendered the Pennzoil Quaker State holdings on October 8, 2002 at a price of $113.099. The tender was accepted with a settlement date of November 1, 2002. On November 4, 2002, the Board received

$9,092,920 in principal and interest plus $240,000 as a consent fee.

Fixed investments are administered through outside vendors. State Street Research and custodial bank Wells Fargo (SSR/WF) managed the fixed assets through December 2001. In December 2001, the State of Montana Section Deferred Compensation Plan transferred all assets from SSR/WF due to a new contract with another investment manager, Pacific Investment Management Company and custodial bank State Street Bank (PIMCO/SSB). The **SSR/WF** portfolio included publicly traded, dollar denominated fixed income securities including U.S. Governments, mortgages, corporates, asset-backed securities, Yankees, and cash equivalents. Private placements issued under rule 144a were permissible. Investments were reported at fair value. State Street Research valued the investment as of the settlement date. Wells Fargo, the custodial bank, valued the investment as of the trade date. The objective was to outperform the total return of the benchmark over a full market cycle, thus providing attractive credited rates to plan participants. Lehman Brothers Intermediate Government/Corporate Index was the benchmark. No more than 5% of the portfolio was allowed to be invested in any issuer at the time of purchase. Each permitted investment category was limited as a percentage of market value of the account in accordance with the investment guidelines. There was no limit on the U.S. Government securities. The fixed investments were transferred to **PIMCO/SSB** under a new contract awarded by the State's competitive bidding process. The PIMCO/State Street Bank fixed investment portfolio is benchmarked against the Lehman Intermediate Government/Credit/Yankee index with a duration not to exceed four years. The minimum average portfolio quality must be an A-rating; the minimum issue quality must be a BB-rating and the minimum commercial paper quality must be A2/P2. The quality ratings applied are the higher of Moody's, Standard and Poor or Fitch. PIMCO has the discretion to invest in a broad array of public and private asset classes and investment vehicles including: money market instruments; U.S. Treasury and Agency notes and bonds; municipal bonds; corporate securities; Yankee and Euro bonds; mortgage-backed securities; mortgage derivatives; asset-backed securities; convertible securities; non-U.S. dollar denominated securities; non-leveraged structured notes; futures; options; swaps; credit default swaps and PIMCO pooled funds. PIMCO may not invest in: caps and floors; preferred stock; emerging market securities; event-linked bonds and bank loans.

Variable investments are held and managed by a selection of retail and institutional mutual funds, which cover all standard asset classes and categories. The selection of offered mutual funds is designed to provide plan participants with the ability to diversify and meet their individual investment goals and strategies. The PERB, with the advice of the statutorily created Employee Investment Advisory Council and the assistance of an independent contracted third-party consultant and investment analyst, conducts an annual review of the offered mutual funds. During the annual review, the PERB may decide to retain, replace or place in a watch status any of the offered mutual funds. The goal of the annual review is to ensure the offered mutual funds meet standards established in the Investment Policy Statement adopted by the PERB. This, in turn, en-

sures plan participants have access to diversified investment options with consistent performance and strategies. A listing of the mutual funds can be obtained by contacting the MPERA.

B. LITIGATION

Each of the plans administered by the PERB may be involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management and legal counsel, the disposition of the matters will not have a material, adverse effect on any plan's financial position as a whole.

C. DEBT OBLIGATIONS

The defined contribution plan has an implementation loan through the Department of Administration that is scheduled to be repaid over a period of 10 years. Five draws were taken in the total amount of $1,498,000. The balance as of June 30, 2001 was $670,000. Draws of $240,000 and $588,000 were taken on November 2, 2001 and June 28, 2002, respectively, and increased the balance of the note payable. Interest repayments began immediately following the draws. Principal repayments begin August 15, 2003, the year following the defined contribution implementation date. The interest rate is variable and changes every February, impacting the interest due on the outstanding principal balance. The MPERA has no other long-term debt. Debt service requirements (principal & interest) for the defined contribution plan is as follows:

Schedule of Debt Repayment

Fiscal Year Ended	Rate*	Principal	Interest	Total
2003	3.150%	$ -	$ 40,590.12	$ 40,590.12
2004	3.150%	181,450.48	45,757.92	227,208.40
2005	3.150%	189,551.35	40,094.01	229,645.36
2006	3.150%	198,050.89	33,942.16	231,993.05
2007	3.150%	206,946.00	27,634.32	234,580.32
2008-2010	3.150%	722,001.28	42,197.26	764,198.54
		$ 1,498,000.00		$ 1,728,215.79

* Interest rate is variable. As of June 30, 2002 the interest rate was 3.150%

D. PLAN MEMBERSHIP, DESCRIPTIONS AND CONTRIBUTION INFORMATION

The plans are established and amended statutorily by the Legislature. In all defined benefit plans (except VFCA), if a member leaves covered employment before retirement, the member contributions plus accrued interest may be refunded to the member. If a member returns to service and repays the withdrawn contributions plus the interest the contributions would have earned had they remained on deposit, membership service is fully restored.

Membership of each plan as of June 30, 2002 and June 30, 2001 is detailed in the charts on the following pages:

PERS Membership	2002	2001		2002	2001
Number of participating employers	515	510			
Active plan members	29,808	29,641	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	13,498	13,195
Vested	2,150	2,015	Disability Retirements	344	332
Non-vested	10,944	10,706	Survivor Benefits	274	271
	13,094	12,721		14,116	13,798

MPORS Membership	2002	2001		2002	2001
Number of participating employers	22	21			
Active plan members	585	580	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	510	506
Vested	18	14	Disability Retirements	15	17
Non-vested	71	65	Survivor Benefits	29	30
	89	79		554	553

GWPORS Membership	2002	2001		2002	2001
Number of participating employers	8	8			
Active plan members	609	521	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	75	74
Vested	9	9	Disability Retirements	1	2
Non-vested	83	81	Survivor Benefits	3	3
	92	90		79	79

SRS Membership	2002	2001		2002	2001
Number of participating employers	56	56			
Active plan members	642	623	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	235	218
Vested	35	26	Disability Retirements	31	30
Non-vested	153	147	Survivor Benefits	14	14
	188	173		280	262

JRS Membership	2002	2001		2002	2001
Number of participating employers	1	1			
Active plan members	48	48	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	49	49
Vested	2	2	Disability Retirements	0	0
Non-vested	0	0	Survivor Benefits	2	2
	50	50		51	51

HPORS Membership	2002	2001		2002	2001
Number of participating employers	1	1			
Active plan members	194	190	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	246	240
Vested	7	8	Disability Retirements	9	10
Non-vested	13	12	Survivor Benefits	10	10
	20	20		265	260

FURS Membership

	2002	2001		2002	2001
Number of participating employers	16	14			
Active plan members	437	425	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	448	439
Vested	6	4	Disability Retirements	6	7
Non-vested	59	57	Survivor Benefits	27	28
	65	61		481	474

VFCA Membership

	2002	2001		2002	2001
Active plan members	2,609	2,524	Retirees and beneficiaries receiving benefits		
Terminated plan members entitled to but not yet receiving benefits or a refund			Service Retirements	880	859
Vested	693	691	Disability Retirements	0	0
			Survivor Benefits	4	3
				884	862

Deferred Compensation (457) Membership

	2002	2001		2002	2001
Number of participating employers	8	8	Number of participating plan members	7,872	7,671
Number of participating employers that provide contributions on members' behalf	1	1	Number of participating plan members that are actively contributing to their deferred compensation accounts	5,319	5,178

Public Employees' Retirement System-DBRP

Plan Description: The PERS-defined benefit retirement plan (DBRP) is a multiple-employer, cost-sharing plan established July 1, 1945, and governed by Title 19, chapters 2 & 3, Montana Code Annotated (MCA). This plan covers the State, university system, local governments and certain employees of the school districts.

Eligible PERS members who are active on July 1, 2002 and all new hires will have a 12-month window during which they may choose to remain in the current PERS-DBRP or join the PERS-DCRP. Members may not be active members of both the defined contribution and defined benefit retirement plans. The choice is irrevocable. Members of the universities also have a third option to join the university system's Optional Retirement Program (ORP). For members that choose to join the PERS-DCRP or the ORP, a percentage of the employer contribution will be used to fund the maintain the funding of the defined benefit plan.

The PERS-DBRP provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are established by state law and can only be amended by the Legislature. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

PERS Summary of Benefits

Member's highest average compensation (HAC)	Highest average compensation during any consecutive 36 months
Years of service required and/or eligible age for benefit	Service retirement: 30 years, any age; Age 60, 5 years of service; or Age 65, regardless of service Early retirement, actuarially reduced: Age 50, 5 years of service; or Any age, 25 years of service
Vesting	5 years
Monthly benefit formula	1.785% of HAC per year of membership service; for members with 25 years of service or more the factor increases to 2%
Guaranteed Annual Benefit Adjustment (GABA)	After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of other adjustments to the member's benefit

At June 30, 2002 PERS had 515 participating employers, an increase of 5 from FY2001. The participating employers consist of:

PERS Employers

Employers	June 30, 2002	June 30, 2001
State Agencies	34	34
Counties	55	55
Cities and Towns	92	90
Colleges and Universities	5	5
School Districts	241	240
Other	88	86
Total	515	510

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2002 was 6.9% of PERS-covered payroll, the same as in fiscal year 2001. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a request for retirement or refund is processed. Each state agency and university system employer contributed 6.9% of PERS-covered payroll during fiscal years 2002 and 2001. Participating local governments and school district employers contributed 6.8% of PERS-covered payroll during fiscal years 2002 and 2001. The State contributed the remaining 0.1% for local governments and school employers from the state general fund in fiscal years 2002 and 2001. A percentage of the employers' contributions is used to fund the employee education program. (Reference Schedule of Contribution Rates on page A-55).

Additional Retirement Benefit: The Legislature enacted a provision (19-2-706, MCA) in relation to the Employee Protection Act (EPA) which allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. As of fiscal year 2002, two hundred forty-seven employees had taken advantage of this provision since its inception, up from two hundred thirty-eight in fiscal year 2001. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. The total retirement incentive contributions received (including interest) during fiscal years 2002 and 2001 totaled $144,782.00 and $228,442.15, respectively. The outstanding balance at June 30, 2002, totaled $342,094.94.

Effective with the July 2001 retirement benefit, some PERS retirees received a purchasing power increase. This increase brings retirees who retired prior to 1982 up to 75% of the purchasing power of their initial retirement benefit. This benefit is in accordance with MCA 19-3-1606.

Public Employees' Retirement System-Education Fund

Education will be provided to the members of PERS-DBRP and PERS-DCRP as governed by section 19-3-112, MCA. The education will be presented with impartial and balanced information about plan choices, investments and retirement planning. The education program will consist of three primary components:
1) initial transfer education – for all active members on the July 1, 2002, plan start date;
2) ongoing transfer education – for new hire members after the July 1, 2002 plan start date; and
3) ongoing investment/retirement planning education – for all active members.

The education program is funded by 0.1% of PERS-covered payroll for fiscal years 2000, 2001 and 2002. Beginning with fiscal year 2003, 0.04% of PERS-covered payroll will be used to fund education.

Municipal Police Officers' Retirement System

Plan Description: The MPORS is a multiple-employer, cost-sharing defined benefit plan that was established in 1974 and is governed by Title 19, chapters 2 & 9 of the MCA. This plan covers all municipal police officers employed by first- and second-class cities and other cities that adopt the plan. Benefits are established by state law and can only be amended by the Legislature. The MPORS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and final average compensation. Member rights for death and disability are vested immediately. All other rights are vested after five years of service. A brief summary of eligibility and benefits follows:

MPORS Summary of Benefits	
Member's final average compensation (FAC)	Hired prior to July 1, 1977 - average monthly compensation of final year of service; Hired after June 30, 1977 - average monthly compensation for last consecutive 36 months
Years of service required and/or age eligible for benefit	20 years, regardless of age; Age 50, 5 years of service
Vesting	5 years
Monthly benefit formula	2.5% of FAC per year of service

MPORS Summary of Benefits (cont.)	
Guaranteed Annual Benefit Adjustment (GABA)	After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit
Guaranteed Minimum Benefit	If hired before July 1, 1997 and member did not elect GABA, the benefit increases to ½ the compensation of a newly confirmed officer in the city that the member was last employed

At June 30, 2002 MPORS had 22 participating employers, an increase of 1 from FY2001. The participating employers consist of:

MPORS Employers

Employers	June 30, 2002	June 30, 2001
Cities and Towns	22	21
Total	22	21

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. Member contribution rates are dependent upon date of hire as a police officer. For fiscal years 2002 and 2001, member contributions as a percentage of salary were 5.8% (if employed on or before June 30, 1975); 7.0% (if employed after June 30, 1975 and prior to July 1, 1979); 8.5% (if employed after June 30, 1979 and prior to July 1, 1997); and, 9.0% (if employed on or after July 1, 1997 and for members electing GABA). Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. City contributions to the retirement plan are 14.41% of total MPORS-covered payroll on a monthly basis. The State contributions are requested at the beginning of the fiscal year based on the previous fiscal year salary and are due no later than November 1. The State's contribution rate for 2002 and 2001 was 29.37%. (Reference Schedule of Contribution Rates on page A-55).

For the MPORS retiree who did not elect the GABA provision, MCA 19-9-1020 provides a one-time benefit increase. This benefit was effective with the May 2001 retirement benefit. The benefit increase is estimated to bring individuals up to 75% of the purchasing power of their initial retirement benefit.

Deferred Retirement Option Plan (DROP): Beginning July 2002, certain members of MPORS who are eligible to retire have the opportunity to participate in the DROP by filing a one-time irrevocable election with the Board. The DROP is governed by Title 19,

Chapter 9, Part 12, MCA. The eligible member must have completed at least 5 years of membership service and reached age 50. The eligible member may participate for a minimum of one month and a maximum of five years. A member may participate in the DROP only once. A participant remains a member of the retirement system, but may not receive membership service or service credit in the system for the duration of the member's DROP period. During the participation in the DROP, all contributions continue to be made to the retirement system. A monthly benefit is calculated based on salary and years of service to the date of the beginning of the DROP period. The monthly benefit accumulates in a DROP account until the end of the DROP period. At the end of the DROP period, the participant receives the balance of the DROP account in a lump-sum payment or in a direct rollover to another eligible plan as allowed by the IRS.

Game Wardens' and Peace Officers' Retirement System

Plan Description: The GWPORS is a multiple-employer, cost-sharing defined benefit plan established in 1963 and is governed by Title 19, chapters 2 & 8, MCA. This system provides retirement benefits to all persons employed as a game warden, warden supervisory personnel, or state peace officer. Benefits are established by state law and can only be amended by the Legislature. The GWPORS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

GWPORS Summary of Benefits	
Member's highest average compensation (HAC)	Highest average compensation during any consecutive 36 months
Years of service required and/or age eligible for benefit	Age 50, 20 years of service; Age 55, 5 years of service
Vesting	5 years
Monthly benefit formula	2.5% of HAC per year of service
Guaranteed Annual Benefit Adjustment (GABA)	After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

At June 30, 2002 GWPORS had 8 participating employers, the same as FY2001. The participating employers consist of:

GWPORS Employers

Employers	June 30, 2002	June 30, 2001
State Agencies	5	5
Colleges and Universities	3	3
Total	8	8

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for the first quarter of fiscal year 2002 and all of fiscal year 2001 was 8.5%. Effective October 1, 2001 the contribution rate increased to 10.56%. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Each state agency and university employer contributed 9.0% of total GWPORS-covered payroll to the retirement plan on a monthly basis, during fiscal years 2002 and 2001. (Reference Schedule of Contribution Rates on page A-55).

Additional Retirement Benefit: The Legislature enacted a provision (19-2-706, MCA) in relation to the Employee Protection Act (EPA) which allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. No employees have taken advantage of this provision to date.

Actuarial Status: Based on current actuarial assumptions the current normal cost is more than the statutory contribution rate; therefore, the system is not actuarially sound. Enacted legislation opened the GWPORS to all state peace officers. The active membership increased from 494 in fiscal year 2000 to 609 in fiscal year 2002. The increase in membership causes the need to reevaluate the actuarial assumptions. Changes to the actuarial assumptions will change the normal cost of the plan. Further research is needed to determine the change in normal cost.

Sheriffs' Retirement System

Plan Description: The SRS is a multiple-employer, cost-sharing defined benefit plan established July 1, 1974, and governed by Title 19, chapters 2 & 7, MCA. This plan provides retirement benefits to all Department of Justice criminal investigators hired after July 1, 1993, and to all Montana sheriffs. Benefits are established by state law and can only be amended by the Legislature. The SRS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits is on the following page:

SRS Summary of Benefits	
Member's highest average compensation (HAC)	Highest average compensation during any consecutive 36 months
Years of service required and/or age eligible for benefit	20 years, regardless of age; Age 50, 5 years of service, actuarially reduced
Vesting	5 years
Monthly benefit formula	2.5% of HAC per year of service
Guaranteed Annual Benefit Adjustment (GABA)	After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit

At June 30, 2002 SRS had 56 participating employers, the same as FY2001. The participating employers consist of:

SRS Employers

Employers	June 30, 2002	June 30, 2001
State Agencies	1	1
Counties	55	55
Total	56	56

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal years 2002 and 2001 was 9.245%. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Each employer contributed 9.535% of total SRS-covered payroll to the retirement plan on a monthly basis, during fiscal years 2002 and 2001. (Reference Schedule of Contribution Rates on page A-55).

Additional Retirement Benefit: The Legislature enacted a provision (19-2-706, MCA) in relation to the Employee Protection Act (EPA) which allows state employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" addi-

tional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. In fiscal year 2002, two employees took advantage of this provision. The total retirement incentive contributions received (including interest) during fiscal year 2002 totaled $44,180. There were no participants or contributions in fiscal year 2001. The outstanding balance at June 30, 2002, totaled $38,083.50.

Judges' Retirement System

Plan Description: The JRS is a single-employer defined benefit plan established in 1967, and governed by Title 19, chapters 2 & 5 of the MCA. This system provides benefits for all Montana judges of the district courts, justices of the Supreme Court, and the Chief Water Judge. Benefits are established by state law and can only be amended by the Legislature. The JRS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

JRS Summary of Benefits	
Member's current salary[1] or highest average compensation (HAC)[2]	[1]Hired prior to July 1, 1997 and non-GABA - monthly compensation at time of retirement; [2]Hired after June 30, 1997 or electing GABA - highest average compensation during any consecutive 36 months
Years of service required and/or age eligible for benefit	Age 60, 5 years of service; Any age with 5 years of service-involuntary termination, actuarially reduced
Vesting	5 years
Monthly benefit formula	3 1/3% of current salary[1] (non-GABA) OR HAC[2] (GABA) per year of service for the first 15 years, plus 1.785% per year for each year after 15 years

JRS Summary of Benefits (cont.)

Guaranteed Annual Benefit Adjustment (GABA)	Hired after July 1, 1997, or those electing GABA, after the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit Hired prior to July 1, 1997, current salary is used in the calculation of the monthly benefit each time the Legislature increases salaries for active judges. This benefit is awarded only to non-GABA members or eligible contingent annuitants

At June 30, 2002 JRS had one participating employer, the same as FY2001. The participating employer consists of:

JRS Employers

Employers	June 30, 2002	June 30, 2001
State Agencies	1	1
Total	1	1

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal years 2002 and 2001 was 7.0% of the member's monthly compensation. Contributions are deducted from each member's salary and remitted by the participating employer. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. As the employer, the State contributed 25.81% of the total JRS-covered payroll to the retirement plan on a monthly basis, during fiscal years 2002 and 2001. (Reference Schedule of Contribution Rates on page A-55).

Highway Patrol Officers' Retirement System

Plan Description: The HPORS is a single-employer, defined benefit plan established July 1, 1971, and governed by Title 19, chapters 2 & 6 of the MCA. This system provides retirement benefits to all members of the Montana Highway Patrol, including supervisory personnel. Benefits are established by state law and can only be amended by the Legislature. The HPORS provides retirement, disability and death benefits to plan members

and their beneficiaries. Benefits are based on eligibility, years of service and highest average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits follows:

HPORS Summary of Benefits	
Member's highest average compensation (HAC)	Highest average compensation during any consecutive 36 months
Years of service required and/or age eligible for benefit	20 years of service, regardless of age; 5 years of service, actuarially reduced from age 60
Vesting	5 years
Monthly benefit formula	2.5% of HAC per year of service
Guaranteed Annual Benefit Adjustment (GABA)	Hired after July 1, 1997, or those electing GABA, after the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit
	Hired prior to July 1, 1997, monthly benefits for non-GABA members are increased each July when they fall below a statutorily guaranteed minimum. Any annual increase is limited to 5% over the current benefit and may not exceed 60% of the current base salary of a probationary officer

At June 30, 2002 HPORS had one participating employer, the same as FY2001. The participating employer consists of:

HPORS Employers

Employers	June 30, 2002	June 30, 2001
State Agencies	1	1
Total	1	1

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rates for fiscal years 2002 and 2001 are 9.05% of the member's total monthly compensation if hired after June 30, 1997 or for members electing GABA and 9.0% for those members hired prior to July 1, 1997 and not electing GABA. Contributions are deducted from each member's salary and remitted by the participating employer. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. As the employer, the State contributed 36.33% of the total HPORS-covered payroll during fiscal years 2002 and 2001. The first 26.15% is payable from the same source used to pay members' compensation. The remaining amount, equal to 10.18%, is payable from a portion of the fees collected from drivers' license and duplicate drivers' license applications. (Reference Schedule of Contribution Rates on page A-55).

Twenty-five cents of each motor vehicle registration fee must be deposited in the HPORS trust fund by the end of each fiscal year. This additional contribution funds the supplemental lump-sum benefit for eligible recipients.

Additional Retirement Benefit: The Legislature enacted a provision (19-2-706, MCA) in relation to the Employee Protection Act (EPA) which allows state and university system employees, who are eligible for a service retirement and whose positions have been eliminated, to have their employer pay a portion of the total cost of purchasing up to three years of "1-for-5" additional service. The employer has up to ten years to complete payment for the service purchases and is charged 8% interest on the unpaid balance. No employees have taken advantage of this provision to date.

Montana highway patrol officers retired prior to July 1, 1991, or their survivors, may be eligible for an annual supplemental lump-sum payment distributed each September. A portion of each motor vehicle registration fee funds this supplemental benefit. Many factors must be considered for eligibility, including the number of years the recipient has received a benefit and the recipient's age. The average annual supplemental payment in fiscal year 2002 was $2,231. In fiscal year 2001, the average annual supplemental payment was $2,162. This enhancement is available to non-GABA recipients only .

Firefighters' Unified Retirement System

Plan Description: The FURS is a multiple-employer, cost-sharing defined benefit plan established in 1981, and governed by Title 19, chapters 2 & 13, MCA. This system provides retirement benefits to firefighters employed by first- and second-class cities and other cities that adopt the plan and to firefighters hired by the Montana Air National Guard on or after October 1, 2001. Benefits are established by state law and can only be amended by the Legislature. The FURS provides retirement, disability and death benefits to plan members and their beneficiaries. Benefits are based on eligibility, years of service and either final monthly compensation or final average compensation. Member rights are vested after five years of service. A brief summary of eligibility and benefits is on the following page:

FURS Summary of Benefits

Member's compensation	Hired prior to July 1, 1981 and not electing GABA - final monthly compensation (FMC); Hired after June 30, 1981 and those electing GABA - final average compensation (FAC) for last consecutive 36 months
Years of service required and/or age eligible for benefit	20 years, regardless of age; Age 50, 5 years of service
Vesting	5 years
Monthly benefit formula	Members hired prior to July 1, 1981 and not electing GABA are entitled to the greater of: 2.5% of FAC per year of service, OR i) if less than 20 years of service, 2% of FMC for each year of service ii) if more than 20 years of service, 50% of the member's FMC plus 2% of the member's FMC for each year of service over 20 years Members hired after June 30, 1981 and those electing GABA: 2.5% of FAC per year of service
Guaranteed Annual Benefit Adjustment (GABA)	After the member has completed 12 full months of retirement, the member's benefit increases by a maximum of 3% each January, inclusive of all other adjustments to the member's benefit For non-GABA members, the monthly retirement, disability or survivor's benefit must be at least one-half the salary of a newly confirmed firefighter employed by the city that last employed the member (provided the member has at least 10 years of service credit). If a benefit falls below that minimum, the benefit is increased and paid to the benefit recipient. If a member or retiree elected GABA, the minimum benefit is not available

At June 30, 2002 FURS had 16 participating employers, an increase of 2 from FY2001. The participating employers consist of:

FURS Employers

Employers	June 30, 2002	June 30, 2001
State Agencies	1	0
Cities and Towns	15	14
Total	16	14

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rates for fiscal years 2002 and 2001 are 9.5% for members hired prior to July 1, 1997, and 10.7% for members hired after June 30, 1997 and members electing GABA coverage. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is established for each member's contributions and interest allocations until a retirement or refund request is processed. Employer contribution rates for fiscal years 2002 and 2001 were 14.36% of the total FURS-covered payroll. The State contribution was 32.61% of total compensation for all covered firefighters in fiscal years 2002 and 2001. State contributions are requested at the beginning of each fiscal year based on previous fiscal year salary and are due no later than November 1. (Reference Schedule of Contribution Rates on page A-55).

Volunteer Firefighters' Compensation Act

Plan Description: The VFCA is a statewide retirement and disability plan. This compensation plan, established in 1965, is governed by Title 19, chapters 2 & 17, MCA. Benefits are established by state law and can only be amended by the Legislature. The VFCA provides pension, disability and death benefits for all volunteer firefighters who are members of eligible volunteer fire companies in unincorporated areas, towns or villages under the laws of the State of Montana. VFCA also provides limited medical expenses for injuries incurred in the line of duty. Benefits are based on eligibility and years of service. Member rights are vested after ten years of credited membership service. A brief summary of eligibility and benefits is on the following page:

VFCA Summary of Benefits	
Years of service required and/or age eligible for benefit	Age 55, 20 years of credited service; Age 60, 10 years of service (partial benefit)
Vesting	10 years
Monthly benefit formula	$7.50 per year of credited service, maximum $150

Contributions: The State is the only contributor to the VFCA. Contributions are 5% of fire insurance premium taxes collected on certain fire risks. The State Auditor makes annual payments from the general fund to the Volunteer Firefighters' Pension Fund from fire insurance premiums. (Reference Schedule of Contribution Rates on page A-55).

Group Insurance Payments: Supplemental payments are available to those volunteer fire companies providing additional group medical insurance for their members in case of death or injury incurred while in the line of duty. The payment is made to the volunteer fire companies and is equal to $75 per year for each mobile firefighting unit owned by the volunteer fire company, up to a maximum of two units.

Public Employees' Retirement System-DCRP

Plan Description: The PERS-defined contribution retirement plan (DCRP) created by the 1999 Legislature and governed by Title 19, chapters 2 & 3, MCA. The PERS-DCRP was available to all active PERS members effective July 1, 2002. The plan began receiving contributions or revenues after the July 1, 2002 implementation date.

The PERB has received a long-term loan from the Montana Department of Administration to fund the plan start-up/implementation costs. Authorization for the loan was provided by the Legislature, Chapter 471, Laws of 1999. As of June 30, 2002, the balance of the five draws taken by the MPERA totals $1,498,000 on this loan. This loan accounts for the negative balance presented on the financial statements. The loan will be paid back over a period of ten years as discussed in Note C of the Financial Section.

Eligible PERS members who were active on July 1, 2002 and all new hires will have a 12-month window during which they may choose to transfer to the PERS-DCRP or remain in the current PERS-DBRP. Members may not be active members of both the defined contribution and defined benefit retirement plans. The choice is irrevocable.

A diverse and broad range of investment options are available to members of the DCRP. The investment options offered within the plan are selected by the PERB with the advice of the statutorily created Employee Investment Advisory Council (EIAC) and with the assistance of a third party consultant and investment analyst. Members of the defined contribution retirement plan will decide how to invest their contributions and a portion of their employer's contributions in the selected investment options. They will be able to invest

in any number of the selected investment options and transfer between options, daily, if desired. The variable investment options cover all standard asset classes and categories. All options range from aggressive to conservative.

The fixed investment option requires the services of three external providers who were selected through the State's competitive bidding process. The external providers are: Aegon, Pacific Investment Management Company (PIMCO) and State Street Bank (SSB). Aegon has a guaranteed investment contract (GIC) that provides a guarantee of principal and sets a quarterly rate of return based upon the investment manager's portfolio yield and duration. PIMCO, the investment manager, directs the investment of fixed assets. Fixed assets are invested in the bond market in accordance with established guidelines for credit quality, duration and issue concentration. SSB is PIMCO's custodial bank and holder of the fixed assets. SSB exchanges the assets as directed by PIMCO.

The remaining portion of employer's contributions will be used to maintain funding of the defined benefit plan, to provide disability benefits and to fund an employee education program. A brief summary of eligibility and benefits follows:

PERS-DCRP Summary of Benefits	
Eligibility for Benefit	Termination of service
Vesting	Immediate for member's contributions and interest; 5 years for employer's contributions and interest
Benefit	Dependent upon individual account balance; IRS permitted rollovers are also possible

Contributions: Member and employer contribution rates are established by state law and may be amended only by the Legislature. The member contribution rate for fiscal year 2003 is 6.9% of member's compensation. The entire amount of the member's contribution is allocated to the member's retirement account. Contributions are deducted from each member's salary and remitted by participating employers. An individual account is maintained by the third-party record keeper. Each state agency and university system employer contributes 6.9% of PERS-covered payroll beginning with fiscal year 2003. Participating local governments and school district employers contribute 6.8% of PERS-covered payroll. The State contributes the remaining 0.1% for local governments and school employers from the state general fund. The employer rate of 6.9% is allocated as follows: 4.19% allocated to the member's retirement account, 2.37% allocated to the defined benefit plan choice rate, 0.04% allocated to defined contribution education fund and 0.3% allocated to the long-term disability plan. (Reference Schedule of Contribution Rates on page A-55).

Deferred Compensation Plan (457)

Plan Description: The State of Montana has offered the deferred compensation plan to employees since 1976. All employees of the State, the Montana University System and contracting political subdivisions, are eligible to participate. The deferred compensation plan is governed by Title 19, chapter 50, MCA in accordance with Internal Revenue Service Code (IRC) §457. As of June 30, 2002 and 2001, the net assets of the deferred compensation plan were $196,420,108 and $200,280,113, respectively.

Assets of the deferred compensation plan are required to be held in trusts, custodial accounts or insurance company contracts for the exclusive benefit of participants and their beneficiaries. Great West Life & Annuity Insurance Co. is the third party record keeper for the deferred compensation plan. Participants elect to defer a portion of their salary, within IRC limits. The deferred salary is not available to employees until separation from service, retirement, death, or upon an unforeseeable emergency while still employed and must meet IRS-specified criteria.

Plan participants direct their deferred salary into investment options offered within the plan. The investment options offered within the plan are selected by the PERB with the advice of the statutorily-created Employee Investment Advisory Council (EIAC) and with the assistance of a third party consultant and investment analyst. Plan participants may invest in as many of the offered investment options as desired. The offered investment options fall into two primary types: (1) the fixed investment option and (2) the variable investment options.

The fixed investment option guarantees both principal (the deferred salary) and a quarterly rate of return. The fixed investment option requires the services of three external providers who were selected through the State's competitive bidding process. The external providers are: Aegon, Pacific Investment Management Company (PIMCO) and State Street Bank (SSB). Aegon has a guaranteed investment contract (GIC) that provides a guarantee of principal and sets a quarterly rate of return based upon the investment manager's portfolio yield and duration. PIMCO, the investment manager, directs the investment of fixed assets. Fixed assets are invested in the bond market in accordance with established guidelines for credit quality, duration and issue concentration. SSB is PIMCO's custodial bank and holder of the fixed assets. SSB exchanges the assets as directed by PIMCO.

The variable investment options include twenty-three mutual funds and five lifestyle/profile funds. All options range from aggressive to conservative. The mutual funds cover all standard asset classes and categories. The lifestyle or profile funds are preset funds that invest in underlying mutual funds to achieve a set objective such as time horizon or investment style.

In addition to the above investment options, plan participants previously had the option to direct a portion of their deferrals to a term life insurance policy provided through Allianz Life Insurance. The ability to invest in life insurance is allowed under the IRC and was offered to plan participants prior to life insurance being offered as a standard component of health insurance benefit packages. This investment option has been discontinued; however, plan participants who had previously or originally elected this option may continue.

Prior to December 28, 2001, the investment managers for the fixed investments were the Montana Board of Investments (BOI) with custodial bank, State Street Bank (SSB); and State Street Research and Management (SSRM) with custodial bank, Wells Fargo. On December 28, 2001, the investments managed by SSRM were transferred to PIMCO and on January 7, 2002, the investments managed by the BOI were transferred to PIMCO.

Administrative expenses and the revenues that fund them are accounted for within the plan. The record keeper charges a fixed administrative fee for all plan participants. The fixed record keeping fee, by contract, is a flat dollar amount. In the interest of equity among varying account balances the flat dollar amount fee is converted to a basis point (or percent) fee based on account balances. This ensures smaller accounts or new plan participants are not incurring more fees than larger accounts or long term plan participants. On a quarterly basis, the contracted record keeper withholds the basis point fee from each plan participant's account. The basis point fees collected are reconciled to the contractual flat dollar amount and any fees withheld in excess of the contractual flat dollar fee are submitted to the PERB. Also submitted to the PERB are 12(b)(1) fees from certain mutual fund companies. 12(b)(1) fees are normally charged by the mutual funds for the purpose of advertising. Because the mutual fund companies involved in the deferred comp plan do not need to advertise to obtain the participants' business the fees are returned to the PERB. The PERB uses the excess and 12(b)(1) fees to pay administrative expenses associated with the deferred compensation plan. These amounts are recorded as Miscellaneous Revenue.

Fees on the fixed investments are charged by each of the three providers. The fees are defined per each contract for specific services rendered. These fees are classified as Investment Expense.

Mutual fund administrative costs are not presented on the financial statements. Mutual fund earnings are generally declared net of expenses in accordance with the SEC and other regulatory authorities. Current reporting standards for mutual companies do not require costs to be made available in the detailed cost reports. A brief summary of eligibility and benefits is on the following page:

Deferred Compensation Plan Summary	
Contribution	Voluntary, tax-deferred
Eligibility for Benefit	Not available to participant until separation from service; retirement; death; or upon an unforeseeable emergency, while still employed and must meet IRS-specified criteria
Vesting	Participants are fully vested in their accounts at the time of deposit
Benefit	Lump sum or periodic benefit payment, at the option of the participant. Based on individual account balances and plan provisions. IRS permitted rollovers are also possible

At June 30, 2002 the deferred compensation plan had 8 participating employers, the same as FY2001. The participating employers consist of:

Deferred Compensation Employers

Employers	June 30, 2002	June 30, 2001
State of Montana*	1	1
Colleges and Universities	6	6
Other	1	1
Total	8	8

* The state of Montana includes 34 agencies; however, due to the nature of the reporting for the 457 plan we are unable to specifically determine which agencies participate.

Contributions: The deferred compensation plan is a voluntary, tax-deferred retirement plan designed to supplement retirement, Social Security and other retirement plans and savings. Participants designate the amount to contribute within IRS limitations. The deferred salary is withheld through payroll deduction prior to federal and state taxes. Social Security and Medicare taxes are withheld on the deferred salary. The contributions are either directed to the fixed investment or to any number of the available variable investments. The money designated as fixed is invested by PIMCO. The money designated as variable is remitted to the third-party record keeper who in turn invests the contributions in selected investments as directed by the participant.

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FY 2002 Schedule of Contribution Rates

System	Member	Employer	State
PERS-DBRP	**6.9%** [19-3-315,MCA]	**6.9%** State & University **6.8%** Local Governments [19-3-316, MCA]	**0.1%** of local government payroll – paid from the General Fund [19-3-319, MCA]
PERS-DCRP[1]	**6.9%** [19-3-315,MCA]	**6.9%** State & University **6.8%** Local Governments [19-3-316, MCA]	**0.1%** of local government payroll – paid from the General Fund [19-3-319, MCA]
MPORS	**5.8%** - hired prior to 07-01-75 & not electing GABA [19-9-710(a), MCA] **7.0%** - hired between 07-01-75 & 06-30-79 & not electing GABA [19-9-710(b), MCA] **8.5%** - hired between 07-01-79 & 06-30-97 & not electing GABA [19-9-710(c), MCA] **9.0%** - hired after 06-30-97 & members electing GABA [19-9-710(d), MCA]	**14.41%** [19-9-703, MCA]	**29.37%** of salaries – paid from the General Fund [19-9-702, MCA]
GWPORS	**10.56%** [19-8-502, MCA]	**9.0%** [19-8-504, MCA]	
SRS	**9.245%** [19-7-403, MCA]	**9.535%** [19-7-404, MCA]	
JRS	**7.0%** [19-5-402, MCA]	**25.81%** [19-5-404, MCA]	
HPORS	**9.0%** - hired prior to 07-01-97 & not electing GABA **9.05%** - electing GABA & new hires after 06-30-97 [19-6-402, MCA]	**26.15%** [19-6-404(1), MCA] **10.18%** of salaries – paid from drivers' license fees [19-6-404(2), MCA]	
FURS	**9.5%** - hired prior to 07-01-97 & not electing GABA [19-13-601(2)(a), MCA] **10.7%** - electing GABA & new hires after 06-30-97 [19-13-601(2)(b), MCA]	**14.36%** [19-13-605, MCA]	**32.61%** of salaries – paid from the General Fund [19-13-604, MCA]
VFCA			**5.0%** of fire insurance premiums, paid by the General Fund [19-17-301, MCA]

[1] Contributions do not begin until after July 1, 2002, the plan implementation date.

Public Employees' Retirement Board

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Schedule of Funding Progress

(in thousands)

System	Actuarial Valuation Date	Actuarial Value of Assets [1] (a)	Actuarial Accrued Liability (AAL) -Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
PERS [2]	06/30/98	$2,128,065	$ 2,300,328	$ 172,263	92.51%	$ 660,579	26.08%
	06/30/00	2,843,347	2,273,407	(569,940)	125.07	725,692	-78.54
	06/30/02	**3,076,781**	**3,077,764**	**983**	**99.97**	**808,747**	**0.12**
MPORS	06/30/98	94,908	173,642	78,734	54.66	17,873	440.52
	06/30/00	129,826	181,109	51,283	71.68	20,252	253.22
	06/30/02	**143,516**	**226,827**	**83,311**	**63.27**	**22,229**	**374.79**
GWPORS	06/30/98	23,190	22,412	(778)	103.47	7,839	-9.92
	06/30/00	32,966	23,922	(9,044)	137.81	11,875	-76.16
	06/30/02	**38,730**	**39,109**	**379**	**99.03**	**17,151**	**2.21**
SRS	06/30/98	92,160	81,077	(11,083)	113.67	20,127	-55.07
	06/30/00	126,338	87,836	(38,502)	143.83	21,559	-178.59
	06/30/02	**138,590**	**121,625**	**(16,965)**	**113.95**	**24,521**	**-69.19**

Analysis of the dollar amounts of plan net assets, actuarial accrued liability, and unfunded actuarial accrued provides one indication of the plan's funding status on a going-concern basis. Analysis of this percentage percentage, the stronger the plan. Trends in the unfunded actuarial accrued liability and annual covered covered payroll approximately adjusts for the effects of inflation and aids analysis of the plan's progress stronger the plan.

[1]Refer to the "Notes to the Required Supplementary Information" for the Actuarial Assest Valuation Method (Page A-62).

[2]PERS Actuarial Valuation revised per audit recommendation.

System	Actuarial Valuation Date	Actuarial Value of Assets[1] (a)	Actuarial Accrued Liability (AAL) -Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
JRS	06/30/98	$ 31,646	$ 29,017	$ (2,629)	109.06%	$ 3,144	-83.62%
	06/30/00	42,043	27,365	(14,678)	153.64	3,483	-421.42
	06/30/02	**44,963**	**30,882**	**(14,081)**	**145.60**	**4,000**	**-352.03**
HPORS	06/30/98	59,531	78,722	19,191	75.62	6,201	309.48
	06/30/00	77,810	76,397	(1,413)	101.85	6,952	-20.33
	06/30/02	**81,734**	**94,850**	**13,116**	**86.17**	**7,536**	**174.04**
FURS	06/30/98	89,988	169,006	79,017	53.25	15,104	523.15
	06/30/00	123,492	162,329	38,837	76.08	16,549	234.68
	06/30/02	**136,392**	**197,946**	**61,554**	**68.90**	**17,953**	**342.86**
VFCA	06/30/98	13,941	18,354	4,412	75.96	N/A	N/A
	06/30/00	17,769	16,752	(1,017)	106.07	N/A	N/A
	06/30/02	**19,254**	**26,808**	**7,554**	**71.82**	**N/A**	**N/A**

Covered payroll is not applicable to VFCA because members are unpaid volunteers.

liability in isolation can be misleading. Expressing plan net assets as a percentage of the actuarial accrued liablity over time indicates whether the plan is becoming financially stronger or weaker. Generally, the greater this payroll are both affected by inflation. Expressing the unfunded actuarial accrued liability as a percentage of annual made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the

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Public Employees' Retirement Board

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Schedule of Employer Contributions & Other Contributing Entities

System		Year Ended June 30	Annual Required Contribution	Percentage Contributed	Annual Required State Contribution [1]	Percentage Contributed
PERS		1997	$ 43,182,090	101.26%	-	-
	2	1998	45,690,886	99.26%	$ 303,840	100.00%
		1999	46,783,993	101.62%	341,099	100.00%
		2000	49,347,082	98.74%	347,560	100.00%
		2001	52,460,464	101.43%	382,481	100.00%
		2002	**54,994,798**	**101.01%**	**373,721**	**100.00%**
MPORS		1997	2,415,188	100.27%	4,939,713	100.00%
		1998	2,575,528	102.33%	5,264,852	100.00%
		1999	2,731,079	99.01%	5,566,398	100.18%
		2000	2,918,274	100.57%	5,947,932	99.35%
		2001	3,011,475	100.12%	6,137,893	100.16%
		2002	**3,203,173**	**102.15%**	**6,528,604**	**100.02%**
GWPORS		1997	242,379	103.16%		
	2	1998	734,502	111.40%		
		1999	891,602	104.42%		
		2000	1,068,745	102.92%		
		2001	1,339,308	101.98%		
		2002	**1,543,547**	**103.33%**		
SRS		1997	1,617,568	104.01%		
	2	1998	1,923,069	102.41%		
		1999	1,994,769	104.36%		
		2000	2,055,688	106.84%		
		2001	2,159,464	103.14%		
		2002	**2,338,104**	**102.10%**		

Refer to the "Notes to the Required Supplementary Information" (Page A-62).

[1] PERS State Contribution of 0.1% for local governments is based on actual receipts for the fiscal year.

[2] A change was made to FY1998 for PERS, GWPORS and SRS to correct contributions erroneously reported in FY1998.

Public Employees' Retirement Board

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Schedule of Employer Contributions & Other Contributing Entities (Continued)

System		Year Ended June 30	Annual Required Contribution[3]	Percentage Contributed	Annual Required State Contribution	Percentage Contributed
JRS		1997	$ 177,181	100.00%		
	1	1998	843,065	100.00%		
		1999	822,795	100.00%		
		2000	899,056	100.00%		
		2001	943,532	100.00%		
		2002	**1,032,319**	**100.00%**		
HPORS		1997	2,282,564	100.17%		
	1	1998	2,336,018	102.52%		
	2	1999	2,293,662	100.65%		
		2000	2,525,631	101.26%		
		2001	2,670,900	98.91%		
		2002	**2,737,999**	**101.16%**		
FURS		1997	2,082,389	99.72%	$ 4,728,879	98.18%
		1998	2,168,902	98.77%	4,925,341	97.37%
		1999	2,262,645	100.94%	5,138,222	98.77%
		2000	2,376,392	97.86%	5,396,528	97.80%
		2001	2,401,328	98.81%	5,453,155	98.45%
		2002	**2,578,021**	**97.80%**	**5,854,406**	**98.46%**
VFCA		1997			910,692	100.00%
		1998			928,484	100.00%
		1999			944,434	100.00%
		2000			961,306	100.00%
		2001			1,002,992	100.00%
		2002			**1,133,741**	**100.00%**

Refer to the "Notes to the Required Supplementary Information" (Page A-62).

[1] A change was made for JRS and HPORS to correct contributions erroneously reported in FY1998.

[2] A change was made for HPORS to correct contributions erroneously reported in FY1999 that should have been FY1998.

[3] For HPORS, the License Fee was moved to Annual Required Contribution for all years presented.

Annual Required District Court Fees	Percentage Contributed	Annual Required Supreme Court Fees	Percentage Contributed	Annual Required Registration Fees	Percentage Contributed
$ 1,024,995	57.84%	$9,869	100.00%		
N/A	N/A	N/A	N/A		
N/A	N/A	N/A	N/A		
N/A	N/A	N/A	N/A		
N/A	N/A	N/A	N/A		
N/A	**N/A**	**N/A**	**N/A**		
				$ 287,284	100.00%
				281,874	100.00%
				285,095	100.00%
				279,577	100.00%
				335,107	100.00%
				308,973	**100.00%**

Public Employees' Retirement Board

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Notes to the Required Supplementary Information

The Information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of latest actuarial valuation follows:

	PERS	MPORS	GWPORS
Valuation date	June 30, 2002	June 30, 2002	June 30, 2002
Actuarial cost method	Entry Age	Entry Age	Entry Age
Amortization method	Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of payroll, open
Remaining amortization period in years:			
Unfunded Liability [1]	0.1	19.6	30
Unfunded Credit [2]			
Asset valuation method	4-Year smoothed market	4-Year smoothed market	4-Year smoothed market
Actuarial assumptions:			
Investment rate of return Compounded annually	8%	8%	8%
Projected salary increases			
Inflation	4.50%	4.50%	4.50%
Merit	0% - 6%	0% - 7.3%	0% - 7.3%
Benefit Adjustments			
GABA	3% after 1 yr	3% after 1 yr	3% after 1 yr
Non-GABA	None	50% newly confirmed officer	None

[1] The unfunded liability for GWPORS is being amortized over 30 years. The current statutory rate is not sufficient to cover normal cost plus amortize the current unfunded liability.
[2] Assets are larger than the past service liability – creating an unfunded credit; the credit is amortized over future costs.

SRS	JRS	HPORS	FURS	VFCA
June 30, 2002	June 30, 2002	June 30, 2002	June 30, 2002	June 30, 2002
Entry Age	Entry Age	Entry Age	Entry Age	Entry Age
Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of payroll, open	Level percentage of revenue, open
30	30	8.7	13.8	21
4-Year smoothed market	4-Year smoothed market	4-Year smoothed market	4-Year smoothed market	4-Year smoothed market
8%	8%	8%	8%	8%
4.50% 0% - 7.3%	4.50% None	4.50% 0% - 7.3%	4.50% 0% - 7.3%	None None
3% after 1 yr None	3% after 1 yr Annual increase to salary of active member in like position	3% after 1 yr 2% per yr service for newly confirmed officer	3% after 1 yr 50% newly confirmed officer	None None

Public Employees' Retirement Board

A Component Unit of the State of Montana

Supporting Schedule

Schedule of Administrative Expenses

Year Ended June 30, 2002

	Defined Benefit Plans	Defined Benefit Education Fund	Defined Contribution PERS-DCRP	Defined Contribution 457 Plan
Personal Services				
Salaries	$ 731,762	$ 90,552	$ 119,002	$ 102,276
Board Members' Per Diem	4,941	899	3,498	1,112
Employee Benefits	191,629	22,994	29,649	26,899
Total Personal Services	928,332	114,445	152,149	130,287
Other Services				
Consulting Services	534,273	1,305,185	185,043	33,890
Legal Fees and Court Costs	10,528	5	1,366	406
Payroll Fees	4,590	558	472	389
Audit Fees	16,700	271	229	203
Medical Services	9,653			
Microfilming	2,356			
Records Storage	3,616	14	17	17
Pre Retirement Seminars	2,500			
Computer Processing	126,474	4,170	18,615	4,929
Printing and Photocopy Charges	48,636	15,364	2,131	8,069
Warrant Writing Services	39,048			
Other	10,639	1,280	1,088	903
Total Other Services	809,013	1,326,847	208,961	48,806
Communications				
Recuitment Costs	305	24	24	24
Postage and Mailing	83,321	6,826	6,686	6,457
Telephone	18,377	1,274	1,200	1,277
Total Communications	102,003	8,124	7,910	7,758
Other Expenses				
Supplies and Materials	58,968	7,491	7,913	5,276
Travel	19,066	14,092	16,300	11,526
Rent	81,606	10,178	9,920	9,095
Repairs and Maintenance	546	190	186	183
Depreciation/Amortization	462			
Compensated Absences	23,120	145	(1,821)	20,793
Interest Payments			33,936	
Miscellaneous	22,742	3,718	9,644	8,487
Total Other Expenses	206,510	35,814	76,078	55,360
Total Administrative Expenses	$ 2,045,858	$ 1,485,230	$ 445,098	$ 242,211

Public Employees' Retirement Board

A Component Unit of the State of Montana

Supporting Schedule

Schedule of Investment Expenses

Year Ended June 30, 2002

Plan	Investment Manager	Fees
PERS-DBRP	Board of Investments	$ 3,784,820
MPORS	Board of Investments	123,484
GWPORS	Board of Investments	32,431
SRS	Board of Investments	123,497
JRS	Board of Investments	48,184
HPORS	Board of Investments	80,681
FURS	Board of Investments	108,640
VFCA	Board of Investments	21,637
457	State Street Research	68,801
	Wells Fargo	4,962
	PIMCO	165,978
	State Street Bank	12,694
Total Investment Expense		**$ 4,575,809**

Public Employees' Retirement Board

A Component Unit of the State of Montana

Supporting Schedule
Schedule of Consultants
Year Ended June 30, 2002

Individual or Firm	Nature of Service	Amount Paid
Educational Technologies, Inc.	Education Consultants	$ 1,303,089
BearingPoint (formerly KPMG Consulting)	Web Reporting Systems Development	470,272
Computer Consulting Corporation	Computer Programming Services	83,108
Arnerich Massena & Associates, Inc.	Mutual Funds Performance Review	55,543
William M. Mercer, Inc.	DC Implementation Consultants	42,666
Milliman USA	Actuarial Consultant	35,959
Ice Miller	Tax Law Consultant	25,164
Legislative Audit Division, Legislative Branch	Independent Auditors	17,403
Communications & Management Service	Human Resources Consulting	12,925
Lawrence R. McEvoy, MD	Medical Consultant	7,068
Legal Services Division, Department of Justice	Legal Services	3,565
Professional Development Center, Department of Administration	Retirement Planning Seminars	2,500
Comserv, Inc.	Death Information System Services	935

PERB Response

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LEGISLATIVE AUDIT DIV.

PUBLIC EMPLOYEE RETIREMENT ADMINISTRATION

JUDY MARTZ
GOVERNOR

STATE OF MONTANA

(406) 444-3154 TELEFAX (406) 444-5428
TOLL FREE (877) 275-7372

100 N. PARK, SUITE 220
PO BOX 200131
HELENA, MONTANA 59620-0131

January 24, 2003

Scott A. Seacat, Legislative Auditor
Legislative Audit Division
State Capitol
Helena, MT 59650

Dear Mr. Seacat,

We have reviewed the recommendations pertaining to the Financial-Compliance Audit of the Public Employees' Retirement Board for the two fiscal years ended June 30, 2002. Our responses follow:

RECOMMENDATION #1
WE RECOMMEND THE PERB WORK WITH THE DEPARTMENT OF ADMINISTRATION TO ENSURE CONTRIBUTIONS ARE PROPERLY RECORDED ON THE STATE'S ACCOUNTING RECORDS.

> Response: We concur. After MPERA's inquiry to correct this issue in December 2002, the decision regarding transfers has been deferred until the completion of the State's CAFR. This is according to an e-mail on December 18, 2002, between the accounting bureau and LAD.
>
> MPERA was first contacted to change the accounting for the registration fees colleted by the Highway Patrol Officers' Retirement System in February 2002. MCA 15-1-122, titled 'Fund Transfers' changed the source from which the funds were to be paid to the HPORS. Originally, Justice made the payment to the HPORS, the new law requires that the general fund 'transfer' $0.25 for each motor vehicle registered to the HPORS. MPERA was reluctant to change the accounting but on the recommendations of the Legislative Fiscal Division, Justice and direction from the DOA MM 2-02-4 and the DOA accounting bureau it was decided that MPERA would comply with the changes. MPERA was again contacted in April to change the accounting of the license fee in a similar fashion. Again the DOA accounting bureau directed that the license fees should be recorded as transfers according to 61-5-121(a), MCA.

MPERA will work with DOA (and the other agencies) at the earliest possible date to resolve this issue and ensure that the funds are correctly reported on SABHRS as well as in the financial statements.

RECOMMENDATION #2

WE RECOMMEND THE PERB IMMEDIATELY REASSESS THE ASSUMPTIONS AND NORMAL COST FOR THE GAME WARDENS' AND PEACE OFFICERS' RETIREMENT SYSTEM IN ORDER TO INTRODUCE ANY LEGISLATION NEEDED TO ENSURE THE SYSTEM IS ACTUARIALLY SOUND AS REQUIRED BY THE MONTANA CONSTITUTION AND STATE LAW.

Response: We concur, the PERB requested and the actuary has reviewed his findings from the 2002 actuarial valuation of the Game Wardens' and Peace Officers' Retirement System. The actuarial assumptions used for the valuation were based on the Experience Study performed before the time the employees of the Department of Corrections had completely transferred from PERS to GWPORS. We have received information from the Department of Corrections regarding the estimated turnover rate for correctional officers working for the department. This turnover rate is significantly higher than the average turnover rate used in the actuarial valuation. Based on this information the actuary states that the revision to the termination rate is reasonable. With the more accurate turnover rate the funded status of the system would have a slight Actuarial Surplus instead of a slight Unfunded Actuarial Liability. The Normal Cost of the system would be lower than the statutory contribution rate. According to the actuary the current statutory contribution rate is actuarially sound.

We appreciate the opportunity to work with your staff on these issues. I would also like to extend our appreciation to you and your staff for the extra effort put forth to complete our audit.

Sincerely,

Mike O'Connor

Mike O'Connor
Executive Director